



FINANCIAL SERVICES REGULATION

Exchange – International Newsletter

Issue 19 – July 2013

INTRODUCTION

WELCOME

DLA Piper's Financial Services International Regulatory team welcomes you to the nineteenth edition of 'Exchange – International', an international newsletter designed to keep you informed of regulatory developments in the financial services sector.

This issue includes updates from [EUROPE](#), [AUSTRIA](#), [GERMANY](#), [HONG KONG](#), the [UK](#) and the [USA](#).

Please click on the links below to access updates for the relevant jurisdictions.

Our aim is to assist you in providing an overview of developments outside your own jurisdiction which may be of interest to you. In each issue we will also focus on a topic of wider international interest. In this edition, "[In Focus](#)" looks at the implementation of the banking reform bill in France.

Please click on the links below to access updates for the relevant jurisdictions.

Your feedback is important to us. If you have any comments or suggestions for future issues, we would be very glad to hear from you.

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If your colleagues would like to be added to our mailing list to receive future client alerts or newsletters, please email amanda.alldrick@dlapiper.com with their contact details. For recent publications, legal updates and an overview of our Litigation & Regulatory capabilities please see our [global website](#).

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EUROPE



ADOPTION OF CRD IV DIRECTIVE AND THE CAPITAL REQUIREMENTS REGULATION

The [CRD IV Directive](#) and the [Capital Requirements Regulation](#) (“CRR”), the legislation comprising the CRD IV reforms, were adopted by the Council of the EU at first reading on 20 June 2013. The legislation is expected to apply from 1 January 2014.

CRD IV will implement the Basel III reforms in the EU, as well as introducing certain EU-specific reforms including imposing restrictions on bonuses.

The CRD IV package of reforms is a comprehensive review of the EU’s prudential requirements for credit institutions and investment firms, as well as EU legislation relating more generally to credit institutions. It implements the main Basel III reforms in the EU as well as introducing certain EU-specific reforms.

The FCA has also published a [statement](#) which details how the new legislative package will be implemented in the UK.

The CRR contains detailed and prescriptive provisions relating to the single rulebook, including provisions relating to the majority of the Basel III reforms, while the CRD IV Directive contains provisions on issues where the degree of prescription is lower and links with national law are particularly important.

CRD IV implements Basel III-related reforms in the following areas:

- **Quality of capital.** CRD IV will tighten the criteria for components to be recognised as regulatory capital, and in particular will strengthen the definition of common equity (which will be the main component of their Tier 1 capital). The CRD’s provisions on the definition of capital will be simplified and Tier 3 capital abolished.
- **Quantity of capital.** The minimum ratios for common equity and Tier 1 capital will increase to 4.5% and 6% respectively, although the minimum capital ratio will remain at 8%.
- **Capital buffers.** CRD IV introduces two capital buffers, which will apply in addition to the increased common equity and Tier 1 capital ratios:

- **Capital conservation buffer.** This buffer, which comprises 2.5% of risk-weighted assets (RWAs) and should consist of common equity, will limit the ability of a firm to make distributions if its capital ratios fall within the buffer.
- **Countercyclical capital buffer.** This buffer, also consisting of common equity, will increase the capital conservation buffer at the discretion of individual national authorities. Its aim is to require firms to build up a buffer of capital during periods of excessive credit growth.
- **Counterparty credit risk.** CRD IV strengthens the capital requirements for counterparty credit risk (CCR) exposures arising from banks’ derivatives, repo and security finance activities. It also aims to encourage increased use of central counterparties (CCPs) for clearing over-the-counter (OTC) derivatives trades.
- **Credit valuation adjustment (CVA) risk.** CRD IV contains measures intended to address exposures to CVA risk (that is, the risk of deterioration in the creditworthiness of a counterparty).
- **Leverage ratio.** CRD IV sets out the Commission’s initial proposals for the introduction of a leverage ratio, which is likely to be the ratio of Tier 1 capital to total non-weighted assets and off-balance exposures.
- **Liquidity requirements.** CRD IV sets out the Commission’s initial proposals for the introduction of two new liquidity ratios: the liquidity coverage ratio (LCR) and the net stable funding ratio (NSFR). These are intended to encourage banks to hold higher levels of unencumbered, high-quality liquid assets.

CRD IV also addresses issues that do not directly relate to the Basel III reforms, including:

- **Remuneration.** CRD IV imposes a 1:1 ratio on certain bankers’ salary relative to variable pay, which can rise to 1:2 with explicit shareholder approval. It will also require firms to disclose the number of individuals with a total remuneration over a certain threshold (currently proposed at EUR1 million or more in each financial year).



- **Single rulebook.** CRD IV introduces a single set of harmonised prudential rules for banks and investment firms. This means that national options and discretions currently available in the CRD will be removed and member states will only be permitted to apply stricter requirements where these are justified by national circumstances, financial stability grounds, or a bank's specific risk profile.
- **Corporate governance.** CRD IV includes measures intended to strengthen corporate governance arrangements and processes. These relate to the composition of boards, and their role in risk oversight and strategy, as well as strengthening the risk management function within firms.
- **Sanctions.** CRD IV will require member states to apply appropriate administrative sanctions and measures to violations of EU banking legislation and will impose common minimum standards for issues such as the level of fines and the publication of sanctions.
- **Reliance on external ratings.** CRD IV includes measures intended to reduce the reliance by credit institutions on external credit ratings.

COUNCIL OF THE EU PUBLISHES MIFID II PROPOSED GENERAL APPROACH

On 19 June 2013, the Presidency of the Council of the EU published the following documents relating to the MiFID II legislative proposals, all dated 18 June 2013:

- A [proposed general approach](#) to the proposed MiFID II Directive.
- A [proposed general approach](#) to the proposed Markets in Financial Instruments Regulation ("MiFIR").
- A [covering note](#) from the General Secretariat to the Council.

The covering note explains that at a meeting of the Permanent Representatives Committee ("COREPER") on 17 June 2013, a provisional agreement was reached on the proposed general approach set out in the above documents. The General Secretariat invites the Council to confirm the agreement on the general approach at the meeting of the European Economic and Financial Affairs Council (ECOFIN) on 21 June 2013, and invites the Presidency to start negotiations with the European Parliament on the basis of this general approach with a view to reaching an agreement at first reading.

The MiFID II legislative proposals will replace and recast the Markets in Financial Instruments Directive (2004/39/EC) (MiFID).

COMMISSION PUBLISHES REGULATORY TECHNICAL STANDARD ON SUPERVISORY COLLEGES FOR CCPs

On 7 June 2013, the European Commission ("Commission") published a regulatory technical standard ("RTS") on colleges for central counterparties ("CCPs"), as required under EMIR (the Regulation on OTC derivatives, central counterparties and trade repositories (Regulation 648/2012)).

The RTS addresses the operational organisation and governance of supervisory colleges that must be set up to scrutinise the application of a CCP for authorisation under EMIR. The provisions also address issues relating to participation in the college, exchange of information among regulatory authorities, conditions relating to delegation and sharing of tasks by members of the college, and how to determine which are the most relevant currencies (as this is used to decide which central banks should participate in each college).

The RTS will enter into force on the twentieth day following publication in the Official Journal of the EU ("OJ").



The European Securities and Markets Authority (“**ESMA**”) submitted the draft RTS to the Commission in March 2013, and in June 2013 it published additional guidelines relating to written agreements between members of supervisory colleges.

EBA PUBLISHES NEAR-FINAL DRAFT RTS ON OWN FUNDS

On 6 June 2013, the European Banking Authority (“**EBA**”) published the **RTS** on own funds under CRD IV (EBA/RTS/2013/01).

The draft follows the EBA’s April 2012 consultation on own funds (Part One).

The draft RTS covers in particular:

- Common equity Tier 1 capital.
- Additional Tier 1 capital.
- Deductions from common equity Tier 1 capital and from own funds in general.
- General requirements (such as indirect holdings arising from index holdings and supervisory permission for reducing own funds).
- Transitional provisions for own funds in terms of grandfathering.

The EBA also provided feedback on the April 2012 consultation and the opinion of the banking stakeholders group (“**BSG**”).

Once formally adopted, the RTS will be part of the single rulebook aimed at enhancing European regulatory harmonisation and strengthening the quality of capital.

The EBA stresses that the draft RTS remain of a preliminary nature pending publication of the final Capital Requirements Regulation (“**CRR**”) in the Official Journal of the OJ. It is publishing the draft RTS on an exceptional basis to provide institutions with an early insight into the EBA’s views on capital instruments under the new regulatory framework and to give feedback on how it has addressed comments received during the April 2012 consultation. The draft RTS therefore remains subject to final formal adoption by the EBA, a review by the European Commission, and a period of potential objection by the Council of the EU and the European Parliament before it becomes EU law.

ESMA UPDATES Q&AS ON EMIR IMPLEMENTATION

On 6 June 2013, ESMA published an updated set of **questions and answers** (“**Q&As**”) (dated 4 June 2013) on the implementation of EMIR (the Regulation on OTC derivatives, central counterparties and trade repositories) (Regulation 648/2012) (ESMA/685). The Q&As were originally published in March 2013.

ESMA explains that the Q&As are aimed at competent authorities to promote common supervisory approaches and practices in the application of EMIR across the EU. However, they should also help investors and other market participants by providing clarity on EMIR’s requirements.

ESMA includes the date on which each section of the Q&As was last added or amended for ease of reference.

The European Commission published some FAQs on EMIR in November 2012, which were updated in February 2013.



ESMA TECHNICAL ADVICE ON SHORT SELLING REGULATION

On 3 June 2013, ESMA published its [technical advice](#) to the European Commission on the impact of the Short Selling Regulation (Regulation 236/2012) (ESMA/2013/649) (“SSR”).

ESMA’s recommendations include:

- The current reporting and disclosure thresholds are appropriate, and do not need to be changed. ESMA suggests considering some technical improvements in the method for calculating net short positions in shares. It also proposes changes in the information provided to competent authorities and the public through the notifications in the case of actively managed funds and on positions held through convertible bonds or subscription rights.
- For the exemption for market making activities, further clarifications are needed and changes to the Level 1 text may be worth considering. Areas for change include the scope of the exemptions and the conditions for being able to use them, particularly the trading venue membership requirement.
- The provisions for temporary bans when there are significant price falls should be reconsidered with a view to simplification and ensuring more consistency.

In an accompanying [press release](#), Steven Majoor, ESMA Chair, said that the SSR has had some positive effects in terms of enhancing market transparency and reducing risks of settlement failure in EU financial markets. However, he also said that ESMA was subject to severe limitations in terms of available data and practical experience of the SSR in preparing its advice as the SSR only came into effect on 1 November 2012.

ESMA’s technical advice follows the Commission’s request for advice in December 2012. The advice will contribute to the Commission’s report on the review of the SSR, which it is required to present to the European Parliament and the Council of the European Union by 30 June 2013.

EUROPEAN COMMISSION INITIATIVES FOR 2013: MAY 2013 UPDATE ON EXPECTED ADOPTION DATES OF FINANCIAL SERVICES MEASURES

On 3 June 2013, the Commission published an updated document setting out its agenda and timetable for the legislative proposals and non-legislative acts that it expects to adopt between 28 May 2013 and 31 December 2013. The most recent previous version of this document was the April/May 2013 update.

Changes to the April/May 2013 update include the following:

- The proposal for a Directive/Regulation on the reform of the structure of EU banks is scheduled to be published in October 2013, rather than in the third quarter of 2013.
- The proposal for a framework for the regulation of the production and use of indices serving as benchmarks in financial and other contracts is scheduled to be adopted on 17 July 2013, rather than on 11 June 2013.
- The Solvency II Directive (2009/138/EC) level 2 implementing measures are no longer listed in the document. They were due to be adopted in the fourth quarter of 2013 and will now, presumably, be further delayed.
- The delegated Regulation to be made under EMIR concerning fees to be charged to trade repositories is scheduled to be adopted in July 2013, rather than in May 2013.
- The delegated Regulation to be made under EMIR concerning the list of exempted entities is scheduled to be adopted in June 2013, rather than in May 2013.



EUROPEAN PARLIAMENT TO CONSIDER UCITS V AT 1 TO 4 JULY 2013 PLENARY SESSION

On 31 May 2013, the European Parliament updated its [procedure file](#) on the UCITS V legislative proposal.

The procedure file now indicates that the Parliament will consider the legislative proposal in its plenary session to be held from 1 to 4 July 2013. The Parliament had previously indicated that it would consider the legislative proposal in its plenary session to be held from 10 to 13 June 2013.

EUROPEAN PARLIAMENT TO CONSIDER MIFID II LEGISLATIVE PROPOSALS AT 9 TO 12 DECEMBER 2013 PLENARY SESSION

On 31 May 2013, the European Parliament updated its procedure files on the MiFID II legislative proposals.

The [procedure file](#) for the proposed MiFID II Directive and the [procedure file](#) for the proposed MiFIR both indicate that the Parliament will now consider these legislative proposals in its plenary session to be held from 9 to 12 December 2013.

The Parliament had previously indicated that it would consider the legislative proposals in its plenary session to be held from 21 to 24 October 2013.

ESMA APPROVES GLOBAL SUPERVISORY CO-OPERATION AGREEMENTS RELATING TO AIFM DIRECTIVE

On 30 May 2013, ESMA published a [press release](#) relating to global supervisory co-operation on alternative funds.

At its 22 May 2013 meeting, ESMA's Board of Supervisors approved co-operation agreements (also known as memorandum of understanding ("MoUs")) between EU securities regulators with responsibility for supervising alternative investment funds

("AIFs") from all 27 member states and 34 of their global counterparts (including those in the USA, India, Australia, Singapore, Hong Kong and key off-shore jurisdictions such as the Cayman Islands.). ESMA has negotiated the agreements on behalf of all member states' securities regulators, as well as the authorities from Croatia, Iceland, Liechtenstein and Norway.

Although ESMA has negotiated the MoUs centrally, they are bilateral agreements that must be signed between each EU securities regulator and the non-EU authorities. As the actual supervision of alternative investment fund managers ("AIFMs") lies with the national securities regulators, each regulator decides with which non-EU authorities it will sign an MoU. In practice member state regulators will sign up to MoUs with the countries listed in the ESMA press release.

The agreements are a key element in allowing EU securities regulators to efficiently supervise the way non-EU AIFMs comply with the Alternative Investment Fund Managers Directive (2011/61/EU) ("AIFM Directive" or "AIFMD"). They are also a pre-condition in allowing non-EU AIFMs access to EU markets, or to perform fund management activities on behalf of EU managers. These arrangements will apply to non-EU fund managers that manage or market AIFs in the EU, and to EU fund managers that manage or market AIFs in third countries. The arrangements also cover co-operation in the cross-border supervision of depositaries and AIFMs' delegates.

The arrangements will apply from 22 July 2013 (the AIFM Directive implementation deadline), and the MoUs will be made available on ESMA's website in due course.

ESMA is negotiating MoUs with further third countries in the light of the July 2013 deadline.



EUROPEAN PARLIAMENT TO CONSIDER SSM LEGISLATIVE PROPOSALS AT 9 TO 12 SEPTEMBER 2013 PLENARY SESSION

On 30 May 2013, the European Parliament updated the following procedure files on the legislative proposals relating to the establishment of the single supervisory mechanism (“SSM”):

- The [procedure file](#) on the proposed Regulation setting up the SSM by conferring specific tasks on the European Central Bank (“ECB”) concerning policies relating to the prudential regulation of credit institutions (“SSM Regulation”).
- The [procedure file](#) on the proposed Regulation amending the EBA Regulation (Regulation 1093/2010) (EBA Amending Regulation).

Both procedure files now indicate that the Parliament will consider these proposals in its plenary session to be held from 9 to 12 September 2013. They had previously stated that Parliament would consider the proposals at its 20 to 23 May 2013 plenary session.

ECB PUBLISHES MAY 2013 FINANCIAL STABILITY REVIEW

On 29 May 2013, the ECB published its bi-annual [financial stability review](#), dated May 2013, with an accompanying [press release](#).

Since 2004, the ECB has published twice a year the financial stability review which provides an overview of the possible sources of risk and vulnerability to financial stability in the euro area.

In the review, the ECB concludes that financial stability conditions in the Euro area remain fragile. Vulnerabilities in the interaction between sovereigns, banks and the macroeconomy persist. Further concrete action by the public and private sector is needed to durably sever negative feedback loops between distressed sovereigns, increasingly diverging economic growth prospects at the country level, and concerns about the financial soundness of banks.

The following four key risks to Euro area stability are highlighted in the review:

- A further decline in bank profitability. This is linked to credit losses and a weak macroeconomic environment. Continued and prompt progress is needed in proactively tackling bank balance sheet problems.
- Renewed tensions in sovereign debt markets due to low growth and slow reform implementation. Continued momentum is needed towards completing a genuine Economic and Monetary Union (“EMU”), including a full banking union.
- Bank funding challenges in stressed countries. Continued steps at both national and EU levels are needed to tackle the remaining fragmentation in bank funding. Further, bank funding markets will benefit from a predictable and consistent approach to bank supervision and resolution across the EU. The launch of the SSM will be a key milestone in this respect.
- Reassessment of risk premia in global markets. Stable and predictable policies are key to the prevention of such a risk reversal. To reduce the losses of such a possible risk reversal, banks and supervisors should ensure that bank capital buffers are sufficient.

COUNCIL COMPROMISE PROPOSAL ON RRD DATED 15 APRIL 2013

On 29 May 2013, the Presidency of the Council of the EU published a compromise proposal (dated 15 April 2013) relating to the European Commission’s legislative proposal for the Recovery and Resolution Directive (“RRD”).

This compromise proposal follows an earlier Council compromise proposal dated 15 March 2013, which was published in May 2013.

Additions to the original legislative proposal are underlined and additions to the 15 March 2013 compromise proposal are shown in bold.



EBA CONSULTS ON DRAFT RTS ON DETERMINING OVERALL EXPOSURES TO CLIENTS IN RESPECT OF TRANSACTIONS WITH UNDERLYING ASSETS

On 17 May 2013, the EBA published a [consultation](#) on a draft RTS on the determination of the overall exposure to a client or a group of connected clients in respect of transactions with underlying assets (EBA/CP/2013/07).

The draft RTS is required by Article 379 of the proposed CRR. The CRR requires firms to determine their overall exposure to a client or a group of connected clients, in respect of clients to which the institution has exposures through collective investment undertakings (“CIUs”), securitisations, or other transactions where there is an exposure to underlying assets (transactions with underlying assets).

The draft RTS contain rules defining the conditions and methodologies used to determine firms’ overall exposures and also the conditions under which the structure of a transaction does not constitute an additional exposure. The RTS includes specific rules relating to the identification of exposures resulting from transactions with underlying assets, the treatment of funds of funds and the calculation method for the overall exposure to a client, or group of connected clients, resulting from a transaction with underlying assets.

The consultation is based on the text of the CRR as agreed by the Council of the EU and the European Parliament in April 2013. The draft RTS may be amended after consultation to take into account the final CRR text.

The RTS will replace Part II of the guidelines on the large exposures regime published in December 2009 by the Committee of European Banking Supervisors (“CEBS”), the EBA’s predecessor.

Comments can be made on the consultation paper by 16 August 2013. The RTS must be submitted to the European Commission by 1 January 2014.

EBA RECOMMENDS SUPERVISORS TO CONDUCT ASSET QUALITY REVIEWS AND ADJUSTS NEXT EU-WIDE BANK STRESS TEST TIMELINE

On 16 May 2013, the EBA published a [press release](#) announcing that the EBA has agreed on recommendations to supervisors to conduct asset quality reviews on major EU banks.

The objective of the asset quality exercises will be to review banks’ classifications and valuations of their assets to help dispel concerns over the deterioration of asset quality due to macroeconomic conditions in Europe.

The EBA’s recommendations intend to contribute to a more uniform approach in the methodology of the reviews through a set of good practices and to a consistent communication on the outcomes of national exercises.

The press release also states that the EBA has adjusted the timeline of the next EU-wide stress test and will conduct the exercise in 2014 once the asset quality reviews are completed. To ensure transparency and comparability over the years, the EBA will provide, in the second half of 2013, appropriate disclosure on the actual exposures of the EU banking sector.

The EBA’s recommendations and the timeframe for the asset quality reviews and the EU-wide stress test will be published once the timeline of the SSM balance sheet assessment is known, as the EBA wishes to take this into account.

EUROPEAN COMMISSION MEMO ON PRACTICAL IMPLEMENTATION OF EMIR FRAMEWORK TO NON-EU CCPs

On 16 May 2013, the European Commission published a [memo](#) (dated 13 May 2013) on the practical implementation of the framework of EMIR in relation to non-EU CCPs.

The purpose of the memo is to specify how the recognition procedure will be implemented for CCPs that are established outside of the EU and wish to provide services to market participants that are established within the EU.



The memo provides information relating to the following:

- The types of CCPs that are subject to the EMIR recognition procedure.
- The benefits of being recognised under EMIR.
- How the EMIR recognition procedure works.
- The process for the adoption of equivalence decisions.
- The time-line that applies for recognition under EMIR.

The text of the relevant articles of EMIR is set out in an Annex to the memo.

AIFM DIRECTIVE IMPLEMENTING REGULATIONS PUBLISHED IN OJ

On 16 May 2013, the texts of two European Commission implementing Regulations required under the AIFM Directive were published in the OJ:

- The [text](#) of the Commission implementing Regulation (Regulation 447/2013) of 15 May 2013 establishing the procedure for AIFMs which choose to opt in under the AIFM Directive.
- The [text](#) of the Commission implementing Regulation (Regulation 448/2013) of 15 May 2013 establishing a procedure for determining the member state of reference of a non-EU AIFM pursuant to the AIFM Directive.

Article 2 of the implementing Regulations states that both will come into force on the twentieth day following their publication in the OJ and shall apply from 22 July 2013.

COUNCIL OF EU ADOPTS CRA III REFORMS AT FIRST READING

On 13 May 2013, the Council of the EU published a [press release](#) announcing that, in its configuration as the Agricultural and Fisheries Council, it has adopted without discussion the proposed Credit Rating Agencies III Regulation (“**CRA III Regulation**”)

and the proposed Credit Rating Agencies III Directive (“**CRA III Directive**”) (together, “**CRA III**”).

The Council has adopted the texts of the legislation that were published in April 2013. These texts reflect the political agreement on CRA III reached with the European Parliament and the adoption by the Parliament of the CRA III legislation at first reading in January 2013.

The CRA III Regulation will make significant amendments to the CRA Regulation (Regulation 1060/2009) on issues including the reliance of firms on external credit ratings, sovereign debt ratings, the civil liability of CRAs and the independence of CRAs. The CRA III Directive will amend the Occupational Pension Funds Directive (2003/41/EC) (“**IORP Directive**”), the UCITS IV Directive (2009/65/EC) and the AIFMD to require firms not to rely solely or mechanistically on external credit ratings for assessing the creditworthiness of assets.

The legislation is now awaiting publication in the OJ.

EU PROPOSES BANK ACCOUNTING SWITCHING DIRECTIVE

On 8 May 2013, the European Commission published a [draft directive](#) to increase the transparency and comparability of payment account fees, simplify account switching and improve cross-border access to basic payment accounts. The European Banking Federation (“**EBF**”) has voiced “serious concerns” in relation to the proposed rules. The EBF states in its [press release](#) of 8 May 2013, that it agrees with the granting of access to basic bank accounts to the financially excluded, however it disagrees that those accounts should be free.

The proposed Directive includes measures payment service providers (“**PSPs**”) will be required to implement: PSPs must handle account switching within 15 or 30 days; Member states must ensure that at least one PSP offers a basic account to consumers regardless of their member state residence and their financial situation. PSPs must also



provide consumers with a list of fees charged for services and each member state must establish at least one independent comparison website. A simple and effective method of comparison is likely to be seen as a good idea from the consumers' perspective but it does raise the issue of how data for such a website would be collected, verified and regulated given the recent issues surrounding submissions to benchmarks, such as LIBOR and EURIBOR.

Given the PSD and EMD review and legislative proposals in relation to cross-border payments and multilateral interchange fees, the payment services sector is likely to see a rise in costs from implementing these regulatory changes.

EUROPEAN COMMISSION ROADMAP ON PROPOSAL FOR STRUCTURAL REFORM OF EU BANKS

On 6 May 2013, the European Commission published a [roadmap](#) (dated April 2013) for a proposal for a structural reform of EU banks.

Publication of the roadmap follows the Liikanen report, which recommended structural reforms to the EU banking sector and the Commission's consultation on the report, both published in October 2012. The Commission published a summary of responses to the consultation in December 2012.

In the roadmap, the Commission states that it considers it urgent to assess the different structural reform options and to devise an EU framework for action. The main issues under consideration are:

- Determining which activities should be subject to separation requirements. These may include proprietary trading, market-making activities and securities underwriting.

- The nature and extent of the separation and governance of separated entities. In particular, the Commission is considering whether separated activities can be conducted behind a ring-fence in a banking group.
- The exemptions available for certain banks if they meet de minimis criteria and conduct the relevant activities that fall below a specified threshold. The Commission considers that the "vast majority" of banks authorised in the EU will fall below de minimis thresholds.

The Commission has not yet decided whether a regulation, a directive, or a combination of both is the appropriate legal instrument.

The Commission has indicated that it will publish the legislative proposal in the third quarter of 2013.

EUROPEAN COMMISSION ROADMAP ON FRAMEWORK FOR CRISIS MANAGEMENT AND RESOLUTION FRAMEWORK FOR NON-BANK FINANCIAL INSTITUTIONS

On 6 May 2013, the European Commission published a [roadmap](#) (dated April 2013) for a framework for crisis management and resolution for financial institutions other than banks.

Publication of the roadmap follows the Commission's October 2012 consultation on a possible recovery and resolution framework for non-bank financial institutions. These institutions include financial market infrastructures ("FMIs") (that is, CCPs and central securities depositaries ("CSDs")), insurance and reinsurance firms, and other non-bank entities and institutions, including payment systems. The Commission published a summary of responses to the consultation in December 2012.



In the roadmap, the Commission states that it is currently considering its policy options. These options range from a broad framework approach covering non-bank financial institutions generally to more specific provisions and tools aimed at particular sectors. It suggests that the outcome of the October 2012 consultation points towards developing specific tools for particular sectors.

The Commission intends for the framework only to cover systemic entities that are “big, interconnected or central enough in the financial system to cause widespread disruption should they fail”.

The Commission has indicated that it will publish the legislative proposal for the framework in November 2013.

IOSCO CONSULTS ON REGULATION OF RETAIL STRUCTURED PRODUCTS

On 18 April 2013, IOSCO published a [consultation report](#) on the regulation of retail structured products (CR05/13).

Among other things, the report:

- Provides background to the project.
- Describes the work undertaken by the working group on retail structured products of IOSCO’s task force on unregulated markets and products (TFUMP). The work included surveying IOSCO members on the market and the regulatory regime in their jurisdictions. Members also described the regulatory challenges.
- Analyses trends in the retail structured product market.
- Proposes a regulatory toolkit that IOSCO members could use in their regulation of retail structured products.

An accompanying [press release](#) states that the retail structured products work follows concern among IOSCO members about the regulatory challenges the products pose, particularly in the area of investor protection.

IOSCO was especially interested in understanding the market’s drivers for supply-side (that is, issuer and distributor) behaviour and demand-side (that is, investor) behaviour. The working group therefore looked along the market’s value-chain, from issuance to distribution to investment.

The consultation period closed on 13 June 2013. IOSCO intends to publish a final report once it has considered the comments received.

COREPER AGREEMENT ON CREATION OF SINGLE SUPERVISORY MECHANISM COMPROMISE TEXTS

On 18 April 2013, the Council of the EU issued a [press release](#) announcing that COREPER has approved the final compromise texts on the establishment of a SSM for the oversight of credit institutions.

The compromise involves two regulations: the ECB Regulation which confers specific tasks on the ECB concerning policies relating to the prudential supervision of credit institutions (also referred to as the “**SSM Regulation**”), and a further Regulation amending the EBA Regulation (Regulation 1093/2010). The final compromise texts have not yet been published.

COREPER was invited to approve the compromise texts in a [revised note](#) (dated 17 April 2013) from the Council’s General Secretariat. The European Parliament announced the agreement in trilogue on 19 March 2013. Following this, the Council continued to examine the final compromise on the ECB Regulation, in light of further limited amendments presented by the Presidency of the Council of the EU.



Annex I of the revised note sets out a political declaration made at an informal meeting of ministers and central bank governors on 12 April 2013 to accompany the final compromise on the ECB Regulation proposal. Member states reaffirmed “their commitment to the urgent completion of all the agreed elements of banking union, as set out by the European Council, in particular in its conclusions of 13/14 December 2012”. Member states also declared that they are “ready to work constructively on a proposal for treaty change” and that the ECB Regulation should be appropriately adjusted, if necessary.

The Council explains in the press release that a letter will now be sent to the chair of the Parliament’s Economic and Monetary Affairs Committee (“**ECON**”) confirming the Council’s agreement on the EBA Regulation and inform the chair that it has also endorsed the amending regulation on the ECB. If the Parliament approves the EBA Regulation as agreed, the Council will approve both texts without further discussion. The Presidency has confirmed that following finalisation of the two regulations in all languages, it will submit them together for final adoption as a package.

EUROPEAN PARLIAMENT PUBLISHES ADOPTED CRD IV TEXTS

The European Parliament has published the texts of the legislative resolutions that it has adopted on the proposed [CRD IV Directive](#) and the proposed CRR.

The Parliament adopted the texts at first reading on 16 April 2013.

PRA AND FCA STATEMENTS ON CRD IV IMPLEMENTATION TIMETABLE

On 16 April 2013, the Financial Conduct Authority (“FCA”) published a [statement](#) on its website setting out its planned timetable for implementation of the CRD IV package of reforms, although it appears that they are co-ordinating their approaches.

The FCA’s statement is very similar to the [statement](#) issued by the Prudential Regulation Authority (“**PRA**”), also on 16 April 2013. According to the PRA statement, if translations can be completed in time for the legislation to be published in the Official Journal of the EU (“**OJEU**”) before 1 July 2013, implementation of CRD IV will be from 1 January 2014. If the legislation is published in the OJEU after 1 July 2013, implementation will be from 1 July 2014. On the basis of the indicated desire of the EU institutions, the PRA is currently planning on the basis that implementation will take place from 1 January 2014.

To facilitate this, the PRA intends to undertake two consultations on elements of the CRD IV framework:

- The main consultation, which it plans to publish in summer 2013, will set out the changes to the PRA’s rules to reflect the new CRR and to implement the Capital Requirements Directive IV (“**CRD IV**”) and relevant discretions provided in the CRR. The PRA notes that the CRR will, in substance, replace the majority of current capital requirements rules in the PRA Rulebook (which can be found in BIPRU and GENPRU).
- A shorter consultation, which it will conduct before the main consultation, will focus on the specific issues related to the procedure for transitioning, as appropriate, existing waivers.

The two consultations will set out the PRA’s approach to implementation in those areas for which it is responsible. In the meantime, firms are asked to discuss any queries or issues, in the first instance, with their supervisor.

Neither statement makes it clear whether the FCA and PRA intend to consult jointly or separately on implementing the CRD IV reforms. But, it appears that they are co-ordinating their approaches.



JOINT LETTER ON MARGIN REQUIREMENTS FOR NON-CENTRALLY CLEARED DERIVATIVES

On 12 April 2013, the International Swaps and Derivatives Association (“**ISDA**”) published a [joint letter](#) from itself, the Institute of International Finance (“**IIF**”), the Association of Financial Markets in Europe (“**AFME**”) and the Securities Industry and Financial Markets Association (“**SIFMA**”) on margin requirements for non-centrally cleared derivatives.

The letter is addressed to the chairmen of, among others, the Basel Committee on Banking Supervision (“**BCBS**”), IOSCO and the FSB, and is a follow-up to individual responses [published](#) by the authors to the BCBS and IOSCO February 2013 consultation on margin requirements for non-centrally cleared derivatives.

The letter states that, while the authors recognise that the proposals for margin requirements are considered to be “near-final,” they still harbour “grave concerns” regarding the initial margin (“**IM**”) requirements. They ask for the regulatory bodies to consider withdrawing or suspending any IM requirements until their consequences have been fully analysed and clarified.

The letter:

- Describes the authors’ key concerns with the IM proposal, which they consider will have a “significant adverse impact” on the global economy, systemic risk, financial market activity and liquidity, and end-user risk management.
- Suggests that a number of research initiatives, including another quantitative impact study (“**QIS**”), should be undertaken.
- Describes the significant flaws that exist in three major policy concepts that may be “weighing heavily” on the treatment of non-cleared over-the-counter (“**OTC**”) derivatives.

AUSTRIA



THE PROPOSAL FOR A REGULATION ON ALTERNATIVE INVESTMENT FUNDS IN AUSTRIA

Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on AIFMD has to be implemented into national law by 22 July 2013. The AIFMD is a key part of the European Commission's drive to lay the regulatory foundations for a secure financial system that supports and stimulates the real economy.

On 23 April 2013 the draft bill of the Austrian Alternative Investment Fund Manager Act (Alternative Investmentfonds Manager – Gesetz, “**AIFMG**”) was circulated for discussion by the Austrian Ministry. The draft bill also includes a number of supplementary amendments, such as tax relevant provisions. The appraisal period ended on 8 May 2013.

The main objective of the AIFMD is to create a comprehensive and secure framework for the supervision and prudential oversight of AIFMs in the EU. An AIFM is a manager of an alternative investment fund. Next to the managers of hedge funds, managers of private equity and closed-end funds shall also be subject to regulation. In contrast with Germany, which decided to issue a single act covering all types of funds, Austria will have the AIFMG as separate legislation dealing with the alternative investment fund managers. Both, the Investment Fund Act (Investmentfondsgesetz, “**InvFG 2011**”) and the Real Estate Investment Fund Act (Immobilien-Investmentfondsgesetz, “**ImmoInvFG**”) shall accordingly remain in force. However, their regulations on AIF shall be implemented in the AIFMG.

All AIFMs, which fall within the scope of the AIFMG, will need to apply for authorisation with the Austrian Financial Markets Authority (Finanzmarktaufsicht, “**FMA**”). According to the draft bill, AIFM shall have an initial capital of at least EUR 125,000 . Where the value of the managed portfolio exceeds EUR 250 million, additional 0.02% of equity is required; this amount shall not exceed EUR 10 million. The option enabling the AIFM to hold parts of the additional capital requirement in form of a guarantee was not utilized in Austria.

Due to its comprehensive scope of application, the AIFMG will have a great impact on the Austrian financial market. Although market participants urged for a quick implementation of the AIFMD into national law, Austria was very late in this procedure. Market participants wanted to have a clear view on the regulation, as soon as possible, as the AIFMD set out many options for the Member States. Indeed, Austria adopted a very strict approach. It appears from the draft bill, that Austria has not chosen any reliefs. In addition, Austria has even adopted a de facto ban on marketing of AIF to retail investors.

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GERMANY



OBLIGATION OF AN INVESTMENT MANAGEMENT COMPANY TO OBTAIN APPROVAL

Under Section 20 (1) sentence 1 KAGB-E (Draft German Investment Code), the business operations of an investment management company require the written approval of the Federal Financial Supervisory Authority (“BaFin”).

1. Definition of investment management company

Pursuant to Section 17 (1) Sentence 1 KAGB-E, investment management companies are companies that have their registered office and headquarters in Germany and whose business operations involve the management of domestic investment funds, EU investment funds or a foreign AIF.

The term ‘investment management company’ supersedes and expands the current term ‘investment company’ as defined in Section 6 (1) of the German Investment Act.

2. Definition of investment fund¹

Pursuant to Section 1 (1) Sentence 1 KAGB-E an investment fund is any undertaking for collective investment that brings together capital from multiple investors to invest it in the investors’ interests according to a set investment strategy and that is not a business enterprise operating outside the financial sector.

3. UCITS and AIF

Pursuant to Section 1 (2) KAGB-E, undertakings for collective investment in transferable securities (“UCITS”) are investment funds that meet the requirements of the UCITS Directive 2009/65/EC. Pursuant to Section 1 (3) KAGB-E AIF are all those investment funds that are not UCITS.

4. Investment companies

Investment funds in the legal form of an investment stock corporation (“**Investmentaktiengesellschaft**”) or investment limited partnership (“**Investmentkommanditgesellschaft**”) are investment companies under Section 1 (11) KAGB-E. This term includes investment stock corporations with variable capital, investment stock corporations with fixed capital, open-ended investment limited partnerships and closed-ended investment limited partnerships.

5. Management of investment funds

Under Section 17 (1) Sentence 2 KAGB-E, the management of investment funds is deemed to exist only if portfolio management or risk management is carried out for one or more investment funds.

6. Internal and external investment management company

Under Section 17 (2) KAGB-E, an investment management company is either an external investment management company appointed by the investment fund or appointed in the name of the investment fund and, based on this appointment, is responsible for the management of the investment fund (external investment management company), or the investment fund itself if the legal form of the investment fund permits internal management and the executive board or the management of the investment fund decides not to appoint an external investment management company (internal investment management company). In this case the investment fund is admitted as an investment management company.

¹ For the interpretation of the term “investment funds” and thus on the scope of application of the KAGB-E, please also see the draft letter on interpretation of BaFin, Consultation 3/2013.



7. Compulsory legal form of the external investment management company

Under Section 18 (1) KAGB-E, external investment management companies can only be operated in the legal form of a public limited company (“**Aktiengesellschaft**”), a limited liability company (“**Gesellschaft mit beschränkter Haftung**”) or a limited partnership (“**Kommanditgesellschaft**”) in which the personally liable shareholder is solely a limited liability company.

8. No so-called “small AIF investment management company”

Small AIF investment management companies that directly or indirectly manage AIFs with assets totalling less than 100 million Euros are not subject to approval by BaFin. Pursuant to Section 44 (1) KAGB-E they are only obligated to register themselves and submit reports.

STEPS ENTAILED IN FILING THE APPLICATION FOR APPROVAL

1. Granting authorisation (optional)
2. Contacting BaFin as the supervisory authority responsible
3. Compiling the information/documents required for the application for approval as appendices to the application
4. Sending the application by the management (alternatively, by the authorised representative) in the name of the company including appendices informally, in writing and in triplicate to BaFin stating:
 - a) the company name;
 - b) the legal form;

- c) the registered office²;
- d) the object of the business;
- e) the executive bodies including the composition thereof;
- f) the expected date on which business operations will commence

LIST OF THE INFORMATION REQUIRED FOR THE APPLICATION FOR APPROVAL³ INFORMATION ON THE INVESTMENT MANAGEMENT COMPANY:

1. Suitable proof of the funds required for business operations pursuant to Section 25 KAGB-E:
 - a) Initial capital amounting to at least:
 - 300,000 euros, if this involves an internal investment management company; and
 - 125,000 euros, if this involves an external investment management company.
 - b) (Additional) own funds depending on the volume of the fund of at least 0.02 percent of the amount by which the value of the investment fund managed exceeds 250 million euros if the value of the AIF investment management company or the managed investment funds exceed 250 million euros; the total amount of initial capital and the additional own funds demanded may, however, not exceed 10 million euros.

² Cf. also the Notes of BaFin on the approval procedure for an AIF investment management company pursuant to Section 22 KAGB-E (last revised: 22 March 2013).

³ Registered office or headquarters of the investment management company must be located in Germany.



- c) An AIF investment management company is not required to meet the demand for additional own funds of up to 50 percent if one of the following institutions or enterprises has provided a guarantee at the same amount:
 - credit institution within the meaning of the Capital Requirements Regulation (CRR) or insurance companies with their registered office in the EU or in the EEA; or
 - credit institutions or insurance companies with their registered office in a third country with equivalent supervisory conditions in the opinion of BaFin.
 - d) Irrespective of its initial capital and additional own funds the investment management company must furnish proof of cost-dependent own funds at any time which correspond to at least one quarter of the costs of the investment management company reported in the income statement of the last annual financial statements under general administrative expenses and the depreciation, amortisation and write-downs on intangible and tangible assets.
2. Articles of association or company agreement of the AIF-investment management company as a certified photocopy if, as an external capital investment company, it intends to manage public AIFs.
 3. Names of the managing directors. There must be at least two managing directors.
 4. Information for the assessment of the reliability of the managing directors.
 5. Information for the assessment of the (theoretical and practical) competence of the managing directors.
 6. Names of the owners of significant participating interests in the AIF investment management company as well as information on the assessment of their reliability and on the amount of their respective participating interest.
 7. Statement of the facts which indicate a close connection between the AIF investment management company and other natural persons or legal entities. The close connection may not inhibit the proper fulfilment of the supervisory functions of BaFin.
 8. Business plan which apart from the organisational structure of the AIF investment management company (for the orderly conduct of business) must also contain information on how the AIF investment management company intends to perform its duties based on the KAGB.
 9. Information on the remuneration policy and remuneration practice subject to Section 37 KAGB-E.
 10. Information on outsourcing agreements within the meaning of Section 36 KAGB-E in conjunction with Art. 75 ff. of the implementing regulation of the European Commission on the AIFM Directive 2011/61/EU.

INFORMATION ON THE AIF

1. Information on the investment strategies of the AIF, including:
 - a) the types of target funds, if the AIF is a fund of funds;
 - b) the principles applied by the AIF investment management company in connection with the use of leverage; and
 - c) the risk profiles and other features of the AIF, which the AIF investment management company manages or intends to manage with information on member states or third states in which the registered office of such AIF is located or is expected to be located.

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HONG KONG



CFA UPHOLDS SFC'S POWER TO SEEK COMPENSATION FOR INVESTORS WITHOUT A CRIMINAL CONVICTION OR A MARKET MISCONDUCT TRIBUNAL (MMT) FINDING

Securities and Futures Commission V Tiger Asia Management Llc, Sung Kook Hwang Bill, Raymond Park, William Tomita [2013] HKCU 1055

Following the Hong Kong Securities and Futures Commission (“SFC”) investigation in 2009, Tiger Asia Management LLC (New York based company) and two of its officers (together “**Tiger Asia Parties**”, none of them were based in Hong Kong) were alleged to have contravened Hong Kong’s insider dealing and market manipulation law in relation to its dealings in the shares of China Construction Bank Corporation and Bank of China (both listed on the Stock Exchange of Hong Kong Limited) and made substantial notional profits of \$29.9 million and \$8.6 million respectively.

The SFC sought orders and injunction under Section 213 of the Securities and Futures Ordinance (“SFO”) to freeze Tiger Asia’s assets, prohibit the Tiger Asia Parties from trading in listed securities and derivatives in Hong Kong, and unwind the relevant transactions and restore affected counterparties to their pre-transaction positions.

The Tiger Asia Parties argued that the Court had no jurisdiction under section 213 to make findings of contravention of these laws without a pre-existing criminal conviction or a MMT determination. The SFC’s view is that section 213 is a free-standing remedy and it can independently seek remedial and preventative orders separately from criminal or deterrent sanctions.

The Court of First Instance ruled against the SFC. This decision was overturned by the Court of Appeal, which confirmed that the objective of section 213 is to provide valuable tools to the SFC to protect the investing public. The Tiger Asia Parties appealed to the Court of Final Appeal.

The Court of Final Appeal dismissed the challenge by the Tiger Asia parties and held:

- it “simply does not follow” that the creation of criminal and MMT procedures for dealing with market misconduct means that such procedures are intended to be exhaustive for determining whether there has been a contravention;
- the remedies under section 213 of the SFO serve a different purpose from the penalties that can be imposed under the criminal and MMT processes;
- in proceedings under section 213, the SFC acts “not as a prosecutor... but as protector of the collective interests of the persons dealing in the market who have been injured by market misconduct”; and
- the question of whether a person has committed a criminal offence remains entirely a matter for the criminal court and is not a matter that is determined in proceedings under section 213 which are plainly civil proceedings.

This decision confirms the wide powers available to the SFC to combat market misconduct and other offences under the SFO. The decision will also act as a further deterrent to investors, particularly to those operating offshore, from contravening the SFO because of the remedial and injunctive powers available to the SFC under section 213.

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LEGAL CUTOVER TO THE NEW UK REGULATORY REGIME FOR FINANCIAL SERVICES

On 1 April 2013, the Financial Services Authority “FSA” was abolished and the majority of its functions transferred to two new regulators: the FCA and the PRA. On the same date, the Bank of England (“BoE”) took over the FSA’s responsibilities for financial market infrastructures and the Financial Policy Committee (“FPC”), which is a committee of the BOE responsible for the financial stability of the UK, was established on a statutory basis.

The PRA intends to communicate the headline results of this work within the next few weeks.

FCA QUARTERLY CONSULTATION (NO 1)

On 6 June 2013, the FCA published its first quarterly [consultation](#) (CP13/3).

CP13/3 invites comments on proposed amendments to a number of different parts of the FCA Handbook:

- Changes to the Insurance: Conduct of Business sourcebook (“**ICOBS**”) (chapter 2). The FCA proposes some consequential changes to ICOBS to align the rules with the Consumer Insurance (Disclosure and Representations) Act 2012, which came into force on 6 April 2013.
- Mortgage market review (“**MMR**”): Perimeter Guidance Manual (“**PERG**”), professional standards and pipeline (chapter 3). The FCA proposes clarificatory amendments to the Handbook following the MMR. It proposes to amend PERG on what constitutes mortgage advice, and the professional standards requirement in the Training and Competence sourcebook (“**TC**”). It also proposes a transitional provision for certain mortgage applications already being processed when the MMR comes into force (pipeline applications).

- Platforms (chapter 4). The FCA proposes a correction to the Glossary definition of platform service, to include execution-only firms that also arrange for the safeguarding and administration of their customers’ investments. It is also consulting on an updated compatibility statement reflecting new FCA objectives. These proposals were explained in the FCA’s policy statement on payments to platforms and cash rebates to consumers (PS13/1).
- Changes to the TC (chapter 5). The FCA proposes to update the qualification requirements by adding five new qualifications and amending the details of five existing qualifications.
- Enforcement: Alternative Investment Fund Managers Regulations 2013 (“**AIFMUKR**”) (chapter 6). The FCA proposes consequential amendments to the Decision Procedure and Penalties manual (“**DEPP**”) and Enforcement Guide (“**EG**”) following the new and updated processes and powers under the AIFMUKR. The AIFMUKR come into force on 22 July 2013.

Comments on the proposals in chapters 5 and 6 should reach the FCA by 6 July 2013, and comments on all other chapters by 6 August 2013.

FCA UPDATE FOR AIFMS

On 5 June 2013, the FCA updated its news [webpage](#) on the AIFMD.

The webpage explains that the FCA has contacted firms who have expressed an interest in becoming authorised as an AIFM by 22 July 2013. These firms have been provided with draft variation of permission (“**VoP**”) forms and are invited to submit draft applications as quickly as possible.



PRA SPEECH ON CAPITAL REQUIREMENTS FOR BANKS

On 4 June 2013, the PRA published a [speech](#) given by Andrew Bailey, Deputy Governor of the BoE and Chief Executive Officer of the PRA, on the PRA's work to monitor the capital requirements of UK banks.

In his speech, Mr Bailey considered generally the challenges of prudential regulation within the new UK framework and the role of the PRA.

Among other things, Mr Bailey referred to the FPC's March 2013 statement, including a recommendation that the PRA should take steps to ensure that by the end of 2013, major UK banks and building societies hold capital resources equivalent to at least 7% of their risk-weighted assets, and that UK banks had around a £25 billion capital shortfall against that measure at the end of 2012.

Mr Bailey said that the PRA is in discussions with banks on capital requirements, and the PRA board is taking a view on whether for each firm it agrees with the quantum of capital implied by the FPC's figure, and the timing of action it requires from banks. The PRA has not released bank-by-bank numbers because it wants to spend time discussing with each bank its judgement on the need for capital, and the banks' judgement on the action they can take.

FCA TRANSACTION REPORTING GUIDANCE ON DERIVATIVES ADMITTED TO TRADING ON NLX

On 4 June 2013, the FCA published a [statement](#) containing transaction reporting guidance on derivatives admitted to trading on NLX, a new multilateral trading facility ("MTF").

The statement explains that derivatives admitted to trading on NLX are considered to be OTC derivatives for the purposes of transaction reporting obligations and firms should report transactions in these instruments in accordance with the FCA's current guidance for OTC derivatives.

The statement also contains an example of a correct report for a transaction executed on NLX and sets out details about completing the instrument identification field and venue identification field.

FCA PUBLISHES DRAFT VARIATION OF PERMISSION FORM FOR AIF DEPOSITARIES

On 31 May 2013, the FCA published a draft of the [VoP form](#) for depositaries of AIFs, together with a new [webpage](#) relating to the depositaries regime under the AIFMD.

The aim is to gather feedback on the VoP form, and the FCA requests that comments should be submitted by 28 June 2013.

The depositaries webpage contains information on:

- The application process for firms that are not currently authorised as depositaries. In particular, the FCA intends to accept draft applications from unauthorised firms before 22 July 2013 to ensure that applications are processed as quickly as possible. Firms should complete the current standard application pack for wholesale investment firms and append it to the completed draft VoP form.
- The transitional arrangements for firms that are currently authorised and who are able to act as depositaries under Article 21(3) of the AIFMD. Such firms will need to submit their VoP application in good time to meet the deadline of 22 July 2014, when the transitional period ends. The FCA will accept VoP applications from 22 July 2013 onwards.
- How the FCA will implement the transitional arrangements for depositaries. The FCA explains that AIFMs submitting VoP forms will be required to submit depositary information. The FCA will then liaise with the specified depositaries to confirm regulatory responsibilities.



FCA NOTE ON SHORT SELLING NOTIFICATION PROCESS FOR MARKET MAKERS AND AUTHORISED PRIMARY DEALERS

On 31 May 2013, the FCA published a [revised note](#) on the UK notification process for market makers and authorised primary dealers relating to the exemption applicable to these entities under Article 17 of the Short Selling Regulation (Regulation 236/2012) (“SSR”).

The note sets out the process for making notifications to the FCA as the UK competent authority for the SSR. It takes into account the guidelines issued by ESMA on the exemption for market makers and authorised primary dealers from the requirement to notify certain levels of net short positions under the SSR. ESMA’s guidelines enter into force on 2 June 2013.

The note supersedes the document published by the FSA in September 2012.

Firms that have already notified the FSA or FCA in order to take advantage of the exemption do not need to notify the FCA again if they intend to continue using the exemption. However, they must notify the FCA if they wish to vary the financial instruments they use the exemption for, or if any changes occur that affect their eligibility, or intention to use, the exemption.

On 28 May 2013, the FCA updated its short selling [webpage](#) with information about a new regime for notifying and disclosing net short positions.

From 10 June 2013, the FCA is introducing:

- A new registration form and requirements for those who have not previously registered to disclose a short position. Persons who have already registered to make notifications or disclosures to the FCA will not be required to re-register.
- One form to make all notifications and disclosures for shares, including correcting or deleting incorrect notifications.

- One form to make all notifications and disclosures for sovereign debt or sovereign credit default swaps, including correcting or deleting previous incorrect notifications.

The short selling webpage was updated on 7 June 2013 to include copies of these new forms and details about the notification process.

NEW FCA APPLICATION AND NOTIFICATION FORMS FOR UK AUTHORISED CISS APPLICABLE FROM 1 JUNE 2013

On 30 May 2013, the FCA updated its collective investment scheme (“CIS”) authorisations team [webpage](#).

From 1 June 2013, the FCA is introducing the following new application and notification forms for UK authorised schemes, which will capture more detailed information at the point of application:

- Form 12: application for an order declaring an investment company with variable capital (“ICVC”) to be authorised.
- Form 242: joint application for an order declaring a unit trust scheme to be authorised.
- Form 21: notification of certain changes for an ICVC under regulation 21 of the Open-Ended Investment Companies Regulations 2001 (SI 2001/1228).
- Form 251: notification of certain changes for an authorised unit trust (“AUT”) under section 251 of the FSMA.
- Form FN: notification of changes to an ICVC or an AUT, following prior approval of the FCA.

The new forms, which take account of many of the questions regularly asked, will help the FCA to progress applications more efficiently. However, these forms do not guarantee that the FCA will not need to ask for further information.



The FCA has also made changes to the submission procedure for UK authorised funds to enable applications and notifications to be submitted electronically, provided certain conditions are satisfied.

The FCA notes that there is no provision in direction 2.1.4 of the Collective Investment Scheme sourcebook (“**COLL**”) for submitting UK authorised fund applications and notifications electronically. However, having regard to the low level of detriment caused to any interested parties by allowing electronic submission, its present position is to allow this method of submission (although this is subject to change). The FCA intends to amend COLL 2.1.4D to provide the option of submitting UK authorised fund applications and notifications electronically. In the meantime, the FCA welcomes views on such a change.

FCA CORPORATE GOVERNANCE FRAMEWORK DOCUMENT

On 24 May 2013, the FCA published a [document](#) summarising its corporate governance framework, which was adopted by the FCA Board on 1 April 2013.

The document contains information about the FCA’s constitution, the role of the FCA Board, the Articles of Association for the FCA, details about matters that are reserved to the FCA Board, and terms of reference for FCA committees.

FCA CONSULTS ON MMR DATA REPORTING REQUIREMENTS

On 15 May 2013, the FCA published a [consultation paper](#) on changes to mortgage data reporting requirements (CP13/2), which are needed to help the FCA supervise changes brought about as a consequence of the FCA’s MMR.

CP13/2 proposes changes to two existing returns that lenders submit once a quarter:

- Product sales data (“**PSD**”). Among other things, the FCA proposes to collect enhanced affordability data and data on the performance of all existing regulated mortgage contracts. It also proposes to make some optional data fields in PSD mandatory to allow meaningful analysis.

- Mortgage lending and administration return (“**MLAR**”). The FCA proposes to collect additional data items from non-deposit taking mortgage lenders, to monitor the prudential position of these firms and their compliance with the new MMR rules.

The draft rules are set out in an appendix to CP13/2 in the Supervision Manual (Product Sales Data and Mortgage Lending and Administration Return) Instrument 2013.

The closing date for responses is 15 August 2013.

The FCA intends to give firms 12 months to implement the changes from the date that the final rules are made, which will “probably” be in the fourth quarter of 2013. Firms would then need to start collecting the new PSD items from the first quarter of 2015 and the FCA will start receiving the data from firms in the second quarter of 2015.

The MMR introduces a package of reforms to the mortgage market, with a focus on responsible lending, that come into effect on 26 April 2014.

FCA UPDATE STATEMENT ON RETAIL DISTRIBUTION OF UCIS AND CLOSE SUBSTITUTES CONSULTATION

On 7 May 2013, the FCA published a statement providing an update on its approach to its August 2012 consultation on proposed restrictions to the marketing of unregulated collective investment schemes (“**UCIS**”) and close substitutes to ordinary retail investors in the UK ([CP12/19](#)).

The FCA had been expected to publish a policy statement setting out its final position in April 2013. However, following discussion with stakeholders, the FCA states that it still has important issues to consider. The FCA is now working towards publishing its final policy statement “as soon as possible” in 2013. The FCA will take account of the later publication date when setting the implementation date for any new rules.

In February 2013, the FSA published a [letter](#) it had sent to firms with an update on its progress regarding CP12/19.



FCA URGES FIRMS TO UPDATE STATUS DISCLOSURES TO REFLECT CREATION OF THE FCA AND PRA

On 1 May 2013, the FCA published a [press release](#) informing firms that it expects them to review their regulatory status disclosures as a priority to ensure they are up to date and accurate following creation of the FCA and PRA and the renaming of the public Financial Services Register.

The FCA explains that where it has been legally able to do so, it has given firms a transitional period for carrying out their updating, for example transitional provisions apply to requirements in the FCA General Provisions sourcebook (“**GEN**”) and in relation to Key Facts documents. However, where obligations derive from European law, the FCA is not able to do this. This includes obligations in the PSRs and in the FCA’s Handbook (for example certain provisions in the Conduct of Business sourcebook (“**COBS**”): COBS 5; COBS 6; COBS 9; and COBS 13).

The FCA recognises that in exceptional circumstances it may not have been possible to make all the required disclosure updates immediately upon the relevant change, but (where transitional provisions are not available) requires firms to be able to demonstrate that they have plans to make these updates at the earliest practical opportunity.

FPC IS GIVEN ITS FIRST REMIT

On 30 April 2013, HM Treasury published a [letter](#) from George Osborne, the Chancellor of the Exchequer, attaching the remit and recommendations for the FPC.

The FS Act, which came into effect on 1 April 2013, requires the government, on an annual basis, to specify its economic policy and to make recommendations to the FPC about matters that the FPC should regard as relevant to its understanding of BoE’s financial stability objective. The FS Act also empowers the government to make recommendations to the FPC about its responsibility relating to support for the government’s economic policy, as well as matters to which the FPC should have regard in exercising its functions.

The remit and recommendations cover the following areas:

- The government’s economic policy objective.
- Matters that the FPC should regard as relevant to the BoE’s financial stability objective, and the FPC’s responsibility in relation to achieving that objective.
- The FPC’s responsibility in relation to support for the government’s economic policy and matters to which the FPC should have regard in exercising its functions. This includes recommendations on the interaction between the FPC’s objectives, recommendations on the interaction between monetary policy and macro-prudential policy, a recommendation that the FPC have regard to risks to public funds, the requirements when making recommendations to HM Treasury on legislative changes to the regulatory perimeters, and accountability.

SANTANDER UK AGREES WITH FCA TO CONTACT MORTGAGE CUSTOMERS ABOUT UNCLEAR MORTGAGE RATE INCREASE INFORMATION

On 19 April 2013, the FCA published a [press release](#) announcing that Santander UK has agreed with the FCA that it will contact over 270,000 mortgage customers about unclear information it gave before increasing the cap on its mortgage standard variable rate (“**SVR**”) in 2008.

An SVR is the mortgage interest rate that many borrowers move to after an introductory deal on products such as fixed rate or tracker mortgages, come to an end. Santander increased its SVR cap margin (that is, its set figure above the BoE bank rate) from 2.5% to 3.75% on 15 December 2008, and was able to charge customers with a mortgage linked to its SVR up to 3.75% above the BoE bank rate, which was 2% at the time.

The FCA believes that the letter sent by Santander to borrowers in 2008 failed to clearly explain the SVR margin increase and its implications. Some customers did not receive



a notification letter at all. Therefore, borrowers may not have understood their options, which for some customers may have included moving to a new lender offering a lower rate or exiting the mortgage without incurring an early repayment charge. The press release states that it is likely that only a minority of borrowers will be entitled to redress, as this will depend on whether they could have moved to a better deal.

Santander has agreed to contact affected customers by letter from 22 April 2013 until autumn 2013. The letter will provide a summary of what happened, what should have happened, and invite the customer to complain, if they have been financially disadvantaged. Santander has also agreed to set up a dedicated telephone line to help customers who may have questions.

LETTER FROM UK AND OTHER GOVERNMENTS TO US TREASURY SECRETARY EXPRESSING CONCERN AT LACK OF PROGRESS IN DEVELOPING CROSS-BORDER RULES ON OTC DERIVATIVES MARKET

On 19 April 2013, HM Treasury published a [letter](#) (dated 18 April 2013) from the UK and certain other governments (as well as the European Commission) addressed to the US Treasury Secretary expressing concern at the lack of progress in developing workable cross-border rules as part of the reform of the OTC derivatives market.

The letter states (among other things) that:

- The signatories are starting to see evidence of fragmentation in the OTC derivatives market, as a result of lack of regulatory co-ordination. The letter attaches a set of principles for cross-border swaps which jurisdictions should carefully consider to avoid cross-border conflicts and support the Pittsburgh G20 reforms.
- Mutual recognition, substituted compliance, exemptions or a combination of these would be a valid approach, and that careful consideration should be given with respect to registration requirements for firms operating across borders.

The letter is signed by the Chancellor of the Exchequer on behalf of the UK government and is also signed by representatives of the French, German, Russian, Brazilian, Swiss, Japanese and South African governments, as well as by Michel Barnier, European Commissioner for Internal Market and Services.

FCA AND PRA PUBLISH RESPECTIVE APPROACHES TO REGULATORY FAILURE

On 19 April 2013, the FCA and PRA each issued their respective approaches to investigating and reporting on regulatory failure, which have been approved for publication by HM Treasury.

Part 5 of the FS Act sets out the tests for determining when each regulator must carry out an investigation into potential regulatory failure and provide reports of its findings and recommendations to HM Treasury. The tests are different for each regulator and relate to their respective statutory objectives. The FCA and PRA papers satisfy a requirement under the FS Act for each regulator to explain how it will meet its statutory requirement to investigate possible instances of regulatory failure and produce a report.

The PRA [policy statement](#) (Conducting statutory investigations) sets out the PRA's policy in this area.

The FCA's statement of policy (which applies from 1 April 2013 for events arising on or after that date) is set out in Annex 1 of its paper, [How the Financial Conduct Authority will investigate and report on regulatory failure](#). The main body of the paper explains the policy in more detail. The FCA explains that it only expects to formally investigate and report in exceptional cases. The FCA will consider whether a failure is serious on a case-by-case basis, and indicates that organisational deficiencies are more likely to constitute a serious failure. Chapter 6 of the FCA paper sets out hypothetical examples of how the policy would apply in practice.



The FCA states that it expects to review the policy after a year of its operation, among other things to take account of the change in scope of the FCA to regulate consumer credit from April 2013. The FCA invites comments on its paper, which it will feed into the review. After the initial review, the statement of policy will be reviewed “periodically”, in particular when the FCA makes changes to its risk framework. The rationale for any changes (which must be consented to by HM Treasury) will be published in the FCA’s annual report.

FSCS CONFIRMS 2013/14 LEVY

On 18 April 2013, the FSCS published a [press release](#), confirming that its proposed levy for 2013/14 will be £285 million.

The final levy is £26 million less than the initial assumptions set out in the FSCS’s [plan and budget 2013/14](#) that were published in February 2013. The reduction follows an up-to-date analysis of claims paid in the previous year and claims assumptions for 2013/14. As a result, all but one class have seen a reduction in the levy compared to the indicative figure. Firms in the investment intermediaries class will see an increase of £2 million in their indicative levy taking their annual levy to £78 million. This is largely because a number of major investment default claims are expected to complete during 2013/14.

The FSCS states that it is expecting the overall volume of new claims it receives to be considerably lower than 2012/13 (28,000 compared to approximately 45,200). The FSCS expects claims volumes in 2013/14 from payment protection insurance (“PPI”) to continue to be significant. The cost of these will fall to the general insurance intermediation sector.

The £285 million levy is in addition to the 2012/13 interim levy that applies to firms in the investment and insurance intermediation classes and which was announced in [March 2013](#).

BANKING REFORM BILL COMPLETES COMMITTEE STAGE IN HOUSE OF COMMONS

On 16 April 2013, the Financial Services (Banking Reform) Bill 2012-13 completed its committee stage in the House of Commons, following the [eighth sitting](#) of the public bill committee for the Bill. A [revised version](#) of the Bill, as amended in the committee stage, is available on the UK Parliament website.

The Bill will now pass to the report stage in the House of Commons.

FCA COMPLAINTS DATA FOR SECOND HALF OF 2012

On 15 April 2013, the FCA published:

- [Aggregated complaints data](#) for the second half of 2012, together with a [press release](#) on the data and [data charts](#).
- [Firm-specific complaints data](#) for the second half of 2012.
- A [press release](#) identifying the firms and products complained most about during the second half of 2012.

During the second half of 2012, the total number of complaints increased by 1%. Complaints for all types of financial products decreased in the second half of 2012 with the exception of general insurance and pure protection contracts (which includes payment protection insurance (“PPI”)). PPI complaints increased by 5% and accounted for 63% of all complaints.

The top five complained about firms in terms of number of complaints opened in the second half of 2012 were Barclays Bank plc, Lloyds TSB Bank plc, Bank of Scotland, MBNA Ltd and Santander UK plc.



The top five complained about financial products in terms of number of complaints opened in the second half of 2012 were PPI, current accounts, other general insurance products (excluding PPI), credit cards and savings and other banking products.

Firms are required to report to the FCA twice a year regarding the number of complaints they receive and how they have handled them. The FSA published [complaints data](#) for the first half of 2012 in September 2012.

FSA POLICY STATEMENT ON NEW FCA HANDBOOK

On 25 March 2013, the FSA published a [policy statement](#) on the new FCA Handbook (PS13/5).

PS13/5 contains the final changes made to the FCA Handbook following consideration of the responses to the FSA's consultations in CP12/24, CP12/26, chapter 2 of CP12/28, CP12/34, CP12/37, CP13/3 and CP13/6. In some cases, the consultations relate to both the FCA and the PRA Handbooks. However, PS13/5 only responds to the proposals that apply to the FCA. The PRA has responded separately on the proposals for which it has responsibility in a policy statement on amendments to the PRA Handbook (PS1/13).

The legal instruments that have been made by the FCA Board are set out in Appendix 3 to PS13/5 and came into effect on 1 April 2013 (legal cutover).

With the exception of the statement of the FCA's approach on qualifying parent undertakings, and the provisions in the instruments that have only been made by the PRA Board, all other rules and guidance published with PS13/5 form part of the FCA Handbook.

FCA'S 2013/14 BUSINESS PLAN AND 2013 RISK OUTLOOK

On 25 March 2013, the FSA published the 2013/14 [business plan](#) and 2013 [risk outlook](#) for the FCA.

The risk outlook sets out the challenging economic backdrop. It also outlines how the FCA will assess market conditions and identify future risks. The FSA explains that many of these are complex and require several years' focus.

The business plan sets out how these risks will be managed in the FCA's first year, and how the FCA will use its resources effectively to meet its objectives to:

- Secure an appropriate degree of protection for consumers.
- Protect and enhance the integrity of the UK financial system.
- Promote effective competition in the interests of consumers.

The key areas of focus for 2013/14 include:

- A renewed focus on consumers. This will include helping to ensure that firms' strategies are aligned with producing appropriate outcomes for consumers (for example, through work on product governance and incentives structures in firms).
- Tackling market abuse, by taking strong enforcement action to deter future misconduct. Focusing on wholesale conduct will be critical for the FCA, as will the new approach to the supervision of trading platforms.
- Ensuring a competitive financial services industry. This is a significant change. It will involve the FCA building a new competition department to embed competition analysis across the organisation. The new department will take action, as appropriate.
- Addressing ongoing misconduct, such as relating to the London Interbank Offered Rate ("LIBOR"), PPI and interest rate swaps.
- Carrying forward major policy initiatives, such as the MMR, the changes to retail investment advice, and extensive engagement with the EU on important directives under consideration.



PRA POLICY STATEMENT ON AMENDMENTS TO THE PRA HANDBOOK

On 25 March 2013, the BoE published a PRA [policy statement](#) on amendments to the PRA Handbook (PS1/13).

PS1/13 contains the final changes made to the PRA Handbook following consideration of the responses to the FSA's consultations in CP12/24, CP12/26, chapter 2 of CP12/28 and CP13/3.

The rules have been made by the board of the PRA and come into effect on 1 April 2013.

FSA AND BOE POLICY STATEMENT ON COMPLAINTS SCHEME FOR THE NEW REGULATORY STRUCTURE

On 25 March 2013, the FSA and the BoE published a joint [policy statement](#) on a scheme for complaints against the FCA, the PRA and the BoE (PS13/7).

PS13/7 summarises feedback received on the joint consultation paper published by the FSA in November 2012 (CP12/30), indicates the regulators' response and contains details of the finalised scheme.

Part 6 of the FS Act requires the FCA, the PRA and the BoE to establish how they will investigate complaints against them. PS13/7 states that the regulators intend to proceed with the consultation proposals, which proposed that the new scheme would operate broadly in line with the FSA's current complaints scheme. The new scheme includes additional processes to enable the regulators to investigate complaints where allegations have been made against more than one of them.

Appendix 1 contains a copy of the finalised complaints scheme. The scheme will no longer be part of the Handbook, but will instead be a standalone document published by the regulators.

The scheme took effect from 1 April 2013.

PRA STATEMENT OF POLICY ON DESIGNATION OF INVESTMENT FIRMS

On 25 March 2013, the BoE published a [policy statement](#) containing a statement of policy on how the PRA will exercise its powers to designate certain investment firms.

Under the FS Act, the PRA will have the power to designate certain investment firms for prudential supervision by the PRA, rather than by the FCA. [The Financial Services and Markets Act 2000 \(PRA-regulated Activities\) Order 2013 \(SI 2013/556\)](#) sets out the criteria that the PRA should apply when considering whether to designate an investment firm.

The Order requires the PRA to issue a statement of policy on designation. In October 2012, the FSA and the BoE published a [consultation](#) on a draft version of the statement of policy.

The policy statement contains a revised version of the statement of policy. The BoE has not made significant changes to the version of the statement consulted on in October 2012. Additional material included in the revised version includes confirmation that:

- When deciding to designate a particular firm, the PRA will take account of its substitutability, interconnectedness and complexity using a range of metrics such as its market share in key markets, legal structure, intra-financial system assets and liabilities and leverage ratio.
- The PRA will discuss individual firms with the FCA as they approach the relevant designation thresholds.



FSA POLICY STATEMENT ON FCA'S USE OF TEMPORARY PRODUCT INTERVENTION RULES

On 25 March 2013, the FSA published a [policy statement](#) (PS13/3) on the approach of the FCA on making temporary product intervention rules (“**TPIR**”).

PS13/3 contains a revised version of the FCA’s statement of policy on making TPIR, which the FCA is required to produce under new section 138N of the FS Act. In December 2012, in [CP12/35](#), the FSA consulted on a draft version of the statement of policy.

Apart from revising the order of the sections within the statement of policy, the FSA has not made significant changes to the version of the statement consulted on in CP12/35. Additional material included in the revised version includes new wording on the FCA Board’s approach to making decisions on TPIR (paragraph 17) and on how firms and consumers affected by a TPIR will be informed (paragraph 38).

PS13/3 also summarises feedback received to CP12/35

The FCA may make revisions to the statement of policy in future and will consult in the normal way on any proposed revisions that it deems to be significant.

FSA POLICY STATEMENT ON THE FCA'S REGULATION AND SUPERVISION OF FIRMS CARRYING ON BENCHMARK-RELATED ACTIVITIES

On 25 March 2013, the FSA published a [policy statement](#) on the FCA’s regulation and supervision of financial benchmarks (PS13/6).

PS13/6 summarises feedback received to the FSA’s December 2012 consultation paper ([CP12/36](#)) and confirms the new rules for firms carrying on regulated activities relating to benchmarks. The only regulated benchmark will be the London Interbank Offered Rate (LIBOR). PS13/6 confirms that two new significant influence controlled functions (“**SIFs**”) will be created under the FCA’s approved persons regime.

Minor modifications and clarifications to the consultation proposals include:

- The financial resource requirements for a benchmark administrator firm will apply independently of any other financial resource requirements that may apply to that firm, and the assets held should be segregated from any group entity.
- Benchmark administrator firms will be required to identify and manage conflicts of interest, and should have sufficient policies to ensure confidentiality of sensitive information, such as proprietary trading information.
- The administrator should have effective procedures for third parties to notify it of any suspicions, and this should be augmented with whistle-blowing procedures.
- The private right of action to seek damages under section 138D of FSMA will not apply to the FCA Handbook rules in MAR 8 for benchmark administrators and those making submissions (submitters).

Appendix 1 of PS13/6 contains a copy of the Benchmarks Instrument 2013 (FCA 2013/33) made on 19 March 2013.

These Handbook provisions came into force on 2 April 2013. The FSA acknowledges that this only allows a short period for firms to implement the new rules, but states that the new rules include provisions to ensure a smooth transition for the individuals nominated to the new controlled functions.



ENFORCEMENT DECISIONS

FCA FINES AND PROHIBITS CHRISTOPHER JOHN RICHES

On 5 June 2013, the FCA published the [final notice](#) it has issued to Christopher John Riches, imposing on him a financial penalty of £63,000 and prohibiting Mr Riches from performing any function in relation to any regulated activity carried on by any authorised person, exempt person or exempt professional firm. The FCA found that Mr Riches was in breach of Principles 1 (Integrity) and 11 (Relations with regulators) of the FCA's Principles for Businesses and section 20 of the Financial Services and Markets Act 2000 Act (the "Act").

Were it not for Mr Riches' financial position the FCA would have imposed on him a financial penalty of £139,851.77 (plus interest). The FCA found that between the period of 12 January 2010 and 30 April 2012, Mr Riches deliberately and for personal benefit conducted regulated activities despite being subject to a requirement, and despite repeated warnings from the FCA, not to do so he deliberately submitted false and misleading information to the FCA and failed to be open and co-operative with the FCA.

FCA FINES IFA NETWORK FIRM £6,031,200 FOR FAILINGS RELATING TO SUITABILITY OF ADVICE AND POOR SYSTEMS AND CONTROLS

On 5 June 2013, the FCA published the [final notice](#) it has issued to Sesame Ltd, an IFA network firm, fining it £6,031,200 for failures relating to the suitability of its advice to clients and systems and controls weaknesses across its investment advice business.

The penalty is made up of a £245,000 fine for Sesame's advice failings in relation to Keydata life settlement products and a £5,786,200 fine for systems and controls weaknesses.

The FCA found that Sesame had breached Principles 3 and 9 of the FCA's Principles for Businesses ("PRIN") in its oversight of its appointed representatives. It found that, between July 2005 and June 2009, Sesame had breached Principle 9 (customers: relationships of trust) as:

- There was a mismatch between many customers' stated investment objectives and attitude to risk and the product sold.
- The suitability letters provided to customers stated incorrectly that income or capital growth was guaranteed.
- Customers were advised incorrectly that certain Keydata products were low risk.

The FCA also found that Sesame failed to take reasonable care to ensure the advice given by its appointed representatives and the decisions they made on behalf of customers were suitable.

The FCA further concluded that between July 2010 and September 2012, Sesame had breached Principle 3 (management and control), as it had failed to take sufficient steps to improve its systems and controls directed at achieving effective oversight of its appointed representatives. These failings meant that the unsuitable sales between 2005 and 2009 could have been repeated in relation to other investment products between July 2010 and September 2012.

In an accompanying [press release](#), Tracey McDermott, FCA Director of Enforcement and Financial Crime, warns firms acting as principals to keep a close eye on their appointed representatives and act decisively when things go wrong.



FCA CANCELS PERMISSIONS OF FIRM FAILING TO MEET THRESHOLD CONDITIONS

On 4 June 2013, the FCA issued a [final notice](#) to Sovereign Financial Solutions Limited (“**Sovereign**”) cancelling the permission granted to Sovereign under the Act. The FCA found that Sovereign failed to satisfy the threshold conditions set out in Schedule 6 to the Act (the “**Threshold Conditions**”). The FCA was not satisfied that Sovereign is a fit and proper person having regard to all the circumstances, including whether Sovereign managed its business in such a way as to ensure that its affairs are conducted in a sound and prudent manner.

The FCA found that has failed to comply with the regulatory requirement to submit its RMAR for the period ended 30 September 2012. Sovereign has not been open and co-operative in all its dealings with the FCA, in that it has failed to respond to the FCA’s repeated requests for it to submit the RMAR, and has thereby failed to comply with Principle 11 of the Authority’s Principles for Businesses and to satisfy the Authority that it is ready, willing and organised to comply with the requirements and standards under the regulatory system.

FCA CANCELS PERMISSIONS OF INDIVIDUAL

On 31 May 2013, the FCA issued a [final notice](#) to Mr John Dixon cancelling his permissions for failing to satisfy the threshold conditions in that the FCA is not satisfied that John Dixon is a fit and proper person having regard to all the circumstances, including whether John Dixon managed his business in such a way as to ensure that his affairs are conducted in a sound and prudent manner.

John Dixon failed to pay regulatory fees and levies owed to the FCA totalling £2,279.63 and he has not been open and co-operative in all his dealings with the FCA, in that he has failed to respond to the FCA’s repeated requests for him to pay the overdue sum, and

has thereby failed to comply with Principle 11 of the FCA’s Principles for Businesses and to satisfy the FCA that he is ready, willing and organised to comply with the requirements and standards under the regulatory system.

FCA PUBLISHES UNDERTAKING BY CLERICAL MEDICAL REGARDING UNFAIR CONTRACT TERMS

On 31 May 2013, the FCA published an [undertaking](#) given by Clerical Medical Investment Group Ltd under the UTCCRs, relating to the fairness of a disclaimer in a form of authority and discharge (FAD).

Customers of Clerical Medical are required to sign a FAD when they apply to transfer their fund to a different provider, or to surrender their funds to buy an annuity. The FCA considers that a disclaimer in the FAD is likely to be unfair because it:

- Has the potential to cause a significant imbalance in the parties’ rights and obligations to the detriment of the consumer. If Clerical Medical relied on this disclaimer against the customer as drafted, it would absolve the firm from all liability. Therefore, a consumer may be deterred from making a valid claim (for example, that their funds had been inappropriately invested or incorrectly calculated).
- Is drafting too broadly. In particular, it does not fulfil the requirement of good faith because the broad wording does not meet the principle of fair and open dealing with consumers.

Clerical Medical has agreed to amend the offending disclaimer to make it clear that customers are not waiving their rights to bring a claim against Clerical Medical for any wrongful act or omission by them. The amended terms are set out in the undertaking. It will treat existing customers as though the new wording applies to them and, from 22 May 2013, introduce the new wording into the FAD.



FCA PUBLISHES UNDERTAKING BY EQUITABLE LIFE REGARDING UNFAIR CONTRACT TERMS

On 31 May 2013, the FCA published an [undertaking](#) given by the Equitable Life Assurance Society under the UTCCRs, relating to the fairness of a disclaimer in a payment instruction form (“**PI form**”).

Customers of Equitable Life are required to sign a PI form when they apply to transfer a life assurance policy, pension fund, savings or investment fund to a different provider, or if they want to surrender a policy or withdraw their money.

The FCA considers that the disclaimer is likely to be unfair because it has the potential to cause a significant imbalance in the parties’ respective rights and obligations to the detriment of the consumer. Customers may be deterred from making valid claims because the disclaimer may have the effect of absolving Equitable Life from all liability under a customer’s original contract. In addition, the broad drafting does not meet the principle of fair and open dealing with consumers and does not fulfil the requirement of good faith.

Equitable Life has agreed to amend the offending disclaimer to make it clear that:

- Equitable Life’s obligation to make payments only ends after it has paid the customer the full lump sum due to them under the policy.
- By signing the PI Form, customers do not waive their right to bring a claim for any other act or omission by Equitable Life.

The amended terms are set out in the undertaking. Equitable Life will treat existing customers as though the new wording applies to them and, from 2 June 2013, introduce the new wording into the PI form.

FCA PUBLISHES DECISION NOTICE BANNING AND FINING FORMER NED FOR CONFLICTS OF INTEREST FAILINGS

On 24 May 2013, the FCA published a [Decision Notice](#) against Angela Burns deciding to fine the former non-executive director (“NED”) £154,800 and ban her from performing any role in regulated financial services for failing to act with integrity as a NED at two mutual societies by failing to disclose her conflicts of interest.

In 2006 Ms Burns completed a consultancy project for a US based investment manager. Shortly after she completed this project Ms Burns asked the investment manager for the opportunity to turn her proposal into a UK business. The investment manager did not take her up on her proposal but she stayed in touch with them. In September 2008, Ms Burns put forward a proposal outlining the consultancy work she could perform for the investment manager. In January 2009 and May 2010, Ms Burns became a NED and chair of the investment committee for two UK mutual societies. Upon taking up her NED positions Ms Burns notified the investment manager of her new roles and renewed her request for consultancy work. Ms Burns did not tell the mutual societies that she was at the same time trying to obtain work from the investment manager and, in the FCA’s opinion, attempted to use her NED positions to benefit herself when she contacted the investment manager. In the FCA’s opinion, Ms Burns had a duty to disclose her interest in seeking consultancy work from the investment manager to her fellow mutual societies’ directors. Ms Burns made no such disclosure.

Consequently, the FSA found that between January 2009 and May 2011, Ms Burns breached Statement of Principle 1 (integrity) of the Statements of Principle and Codes of Practice for Approved Persons (APER) by, among other matters, recklessly, and in breach of her fiduciary position as a NED at the two mutual societies, failing to disclose her conflicts of interest to the mutual societies.

The FSA considered the conduct as serious as Ms Burns fell below the standards expected of a NED and maintained throughout the relevant period that she did not have a conflict of interest. Ms Burns’ actions also caused detriment to the investment manager of the mutual societies.



FCA INTERVENES TO BRING RBS INTEREST RATE SWAPS MISSELLING APPEAL FORWARD

On 16 May 2013, an article on [ftadviser.com](#) reported that following a request from the FCA, the Court of Appeal has brought forward the hearing of the appeal against a verdict in favour of the Royal Bank of Scotland (“RBS”) over an interest rate swaps misselling claim.

The appeal will be heard over two days between 29 and 31 July 2013.

The FSA published a [report](#) setting out its findings from the pilot reviews completed by banks into the misselling of interest rate hedging products to small businesses in January 2013.

FCA IMPOSES FINE ON J.P. MORGAN INTERNATIONAL BANK LIMITED

On 10 May 2013, the FCA published the [final notice](#) it has issued to J.P. Morgan International Bank Limited (“JPMIB”).

The FCA has imposed a financial penalty of £3,076,200 for failing to comply with Principle 3 and SYSC 9.1.1R. During the period of 1 January 2010 and 17 February 2012, JPMIB failed to take reasonable care to organise and control its affairs relating to its provision of retail investment advice and portfolio investment services responsibly and effectively, with adequate risk management systems.

JPMIB agreed to settle at an early stage of the FCA’s investigation. It therefore qualified for a 30% (Stage 1) discount under the FCA’s executive settlement procedures. Were it not for this discount, the FCA would have imposed a financial penalty of £4,394,695 on JPMIB.

FCA ARRESTS TWO INDIVIDUALS IN INSIDER DEALING INVESTIGATION

On 3 May 2013, the FCA published a [press release](#) announcing that a man and a woman have been arrested and questioned in connection with an investigation into insider dealing and market abuse.

The arrests follow the FCA’s execution of a search warrant in West London, with the assistance of the City of London Police Economic Crime Directorate.

The press release states that no individuals have been charged at this time and the arrests are not linked to any other ongoing insider dealing investigation.

Businesses and private premises in Switzerland were also searched by the Swiss authorities in connection with the FCA’s investigation.

FCA CENSURES MONEY TRANSFER COMPANY

On 30 April 2013, the FCA published the [final notice](#) it has issued to Horn Express Ltd (formerly known as Quaran Express Money Transfer Limited), a money transfer company authorised by the FCA under the PSRs.

The FCA has censured Horn for failing to safeguard and segregate customer funds in breach of Regulation 19 of the PSRs (safeguarding requirements). The FCA would have fined the firm £136,687 had the firm not produced verifiable evidence that imposing a fine would have caused it serious financial hardship. This is the first time that a public sanction has been imposed on a payment institution authorised under the PSRs for misconduct under the PSRs (other than for failures to comply with minimum conditions for registration or authorisation).



During the period between 1 December 2009 and 26 August 2011, Horn mixed customer funds with its own monies in the same bank account and failed to record accurately how much of the money in that account was customers' funds. Horn also failed to properly reconcile the customer funds held in its bank account and to set up the bank account properly (for example, it was not labelled as a customer funds account, which meant that customers might have lost their money if Horn had become insolvent). Horn had also failed to sufficiently supervise its branches and agents, and the records of compliance visits that it carried out failed to show an adequate assessment of the safeguarding and segregation requirements for customers' funds.

In an accompanying [press release](#), Bill Sillett, FCA head of retail enforcement, commented that the FCA will use its enforcement powers to the full extent and this case, the first of its kind, demonstrates that the FCA will take action where breaches are identified.

FCA CHARGES TWO IN RELATION TO UNAUTHORISED INVESTMENT SCHEME

On 29 April 2013, the FCA published a [press release](#) announcing that it has charged Alex Hope and Raj Von Badlo with a total of ten offences relating to an unauthorised investment scheme they promoted and operated.

The scheme purported to carry out forex trading for the benefit of investors and is believed to have taken over £5 million from investors.

Both men have been bailed to attend City of London Magistrates Court.

FCA FINES EFG PRIVATE BANK LTD

On 24 April 2013, the FCA published a [final notice](#) it has issued EFG Private Bank Ltd ("EFG") fining EFG £4.2 million for failing to take reasonable care to establish and maintain effective anti-money laundering ("AML") controls for high risk customers. The failings were serious and lasted for more than three years.

The findings come as a result of a FSA thematic review of how UK banks were managing money laundering risk in higher risk situations. The investigation found that EFG had not fully put its AML policies into practice.

EFG agreed to settle at an early stage of the FSA's investigation. The Firm therefore qualified for a 30% (Stage 1) discount under the FSA's executive settlement procedures. Were it not for this discount, the FSA would have imposed a financial penalty of £6,000,000 on EFG.

FCA BANS AND CENSURES MANAGING DIRECTOR OF SIPP OPERATOR

On 18 April 2013, the FCA published the [final notice](#) issued to Kevin Wells, managing director of a self-invested personal pension ("SIPP") scheme operator, for failings relating to operating a SIPP.

The FCA imposed a public censure on Mr Wells for failing to comply with Statements of Principle 6 (due skill, care and diligence) and 7 (compliance with relevant regulatory requirements) of the FCA's Statements of Principle for Approved Persons ("APER"). It also banned Mr Wells from performing any significant influence function relating to any regulated activity.

Mr Wells was approved to perform the CF1 (Director) controlled function at Montpelier Pension Administration Services Ltd ("MPAS"). Between July 2009 and January 2011, the FCA found that Mr Wells' failings meant that, among other things, MPAS:

- Put client money at risk by breaching FCA rules on client assets.
- Failed to vet and monitor third parties, for example the IFAs and fund managers that MPAS dealt with.
- Lacked adequate knowledge of the assets it administered for clients.



The FCA also held that by failing to ensure that MPAS properly assessed the risks associated with accepting esoteric investments into its schemes, Mr Wells potentially exposed scheme members to an increased risk of loss.

In an accompanying [press release](#), Tracey McDermott, FCA Director of Enforcement and Financial Crime, recommends that anybody operating, or thinking of operating, a SIPP reads the final notice in detail as it “covers almost all aspects of SIPP operation and is a good indicator of the standards” that the FCA expects.

FCA CHARGES EIGHT MEN WITH OFFENCES RELATING TO LAND BANKING

On 17 April 2013, the FCA published a [press release](#) announcing that it has charged eight men with conspiracy to defraud and criminal offences relating to the carrying out of a regulated activity (operating a collective investment scheme (CIS)) without authorisation or exemption contrary to the general prohibition in section 19 of FSMA.

The charges arise out of an ongoing FCA investigation into the activities of three land banking companies: Plott UK Limited (“**Plott**”), European Property Investments (UK) Limited (“**EPI**”) and Stirling Alexander Limited. These companies are believed to have taken over £5 million from UK investors between 2008 and 2011. The FCA’s predecessor, the FSA, previously successfully brought civil proceedings against Plott and EPI that resulted in the compulsory winding up of these companies in June 2011 and December 2012 respectively.

Scott Crawley, Daniel Forsyth, Ross Peters, Aaron Petrou, Ricky Mitchie, Dale Walker, Adam Hawkins and Brendan Daley have been bailed to attend City of London Magistrates Court on 10 May 2013.

FSA ISSUES FINAL NOTICES REFUSING IFA’S APPLICATIONS FOR AUTHORISATION AND APPROVAL

On 28 March 2013, the FSA published the [final notice](#) that it has issued to Sidney Cordle and the [final notice](#) issued to Scott Briscoe Limited (“**SBL**”), following the Upper Tribunal’s (Tax and Chancery Chamber) decision in this case.

The case concerned two decision notices issued by the FSA on 20 January 2012, under which the FSA rejected applications made by an IFA, Sidney Cordle for his firm, SBL, to be authorised to carry on regulated activities and for him to be approved to perform controlled functions CF1 (director), CF10 (compliance oversight), CF11 (money laundering reporting officer) and CF30 (customer).

The FSA had based its decision on Mr Cordle’s failure to disclose information in the relevant application forms relating to the nature and outcome of an investigation into SBL carried out by the financial services network, Sesame Ltd, in respect of which SBL had previously been an appointed representative. The FSA considered that this non-disclosure meant that Mr Cordle had failed to demonstrate the required standards of honesty and integrity and was not, therefore, a fit and proper person.

The tribunal found that the FSA had “sound reasons” for rejecting the applications for authorisation and approval and, therefore, upheld the terms of the decision notices.

FSA FINES FINANCIAL ADVISER FOR FAILING TO PROVIDE SUITABLE ADVICE

On 27 March 2013, the FSA published the [final notice](#) it has issued to Care Asset Management Limited (“**Care**”), an independent financial adviser firm.

The FSA has fined Care £56,000 for breaches of Statement of Principle 9 (Customers: relationships of trust) of PRIN. The penalty relates to failings by Care in its sales of products provided by Keydata.



Care focuses on providing advice to customers approaching or in retirement, including customers in care homes. It had failed to provide suitable advice on investment in Keydata products having incorrectly rated the risk of the products, failed to communicate clearly to customers, and failed to have adequate systems in place to ensure it understood the risks its customers were willing to take.

In particular, Care had classified Keydata products as secure on its risk rating list. However, the products had many of the characteristics of other products that had been graded as higher risk on Care's risk rating list.

In addition, Care had failed to have adequate systems in place to ensure it: understood the risks its customers were willing and able to take; provided written documentation to customers adequately describing the nature and risks of the products; and adequately monitored the sale of Keydata products.

The FSA regarded the failings as being particularly serious since (among other things) the potential risk to many of the customers was increased by their age.

FSA FINES PRUDENTIAL GROUP COMPANIES £30 MILLION AND CENSURES CHIEF EXECUTIVE FOR FAILING TO INFORM IT OF ACQUISITION PLANS ON A TIMELY BASIS

On 27 March 2013, the FSA published the [final notice](#) it has issued to The Prudential Assurance Company Limited, fining it £16 million for breaching Principle 11 (relations with regulators) of the FSA Principles for Businesses, the [final notice](#) issued to Prudential plc, fining it £14 million for breaching Listing Principle 6 (dealing with the FSA in an open and co-operative manner), and the [final notice](#) issued to Mr Tidjane Thiam, the group chief executive, for being knowingly concerned in a breach of Principle 11.

In early 2010, Prudential was considering acquiring AIA, an Asian subsidiary of AIG. Prudential failed to disclose the proposed transaction at a meeting with the FSA on 12 February 2010, when the FSA asked detailed questions about Prudential's strategy for

growth in the Asian market and its plans to raise equity and debt capital. Prudential did not inform the FSA about the proposed transaction until after it had been leaked to the media on 27 February 2010. The transaction (from which Prudential withdrew in June 2010) would have transformed Prudential's financial position and strategy and would have involved a rights issue of £14.5 billion, the biggest ever in the UK. As a result of the delay in informing the FSA, the FSA needed to review the proposed transaction from a regulatory perspective within a compressed time scale.

In an accompanying [press release](#), Tracey McDermott, the FSA Director of Enforcement and Financial Crime said: "Firms should be in no doubt as to the importance of early communication with the regulator in respect of transformational transactions to avoid market and investor disruption....This case should send a clear message to all board members of their collective and individual responsibility for the decisions they make on behalf of their companies."

FSA ISSUES FINAL NOTICES TO FINANCIAL ADVISER AND INVESTMENT ADVISORY FIRM

On 26 March 2013, the FSA published the final notices (each dated 22 March 2013) it had issued to [Stephen Hocking](#) and [Pave Financial Management Limited](#).

In the final notice to Mr Hocking, the FSA published a statement of the misconduct of Mr Hocking for his failure to comply with Principles 1 (integrity), 2 (skill, care and diligence) and 7 (compliance with relevant regulatory requirements) of APER.

The FSA withdrew Mr Hocking's approval to perform the controlled functions CF1 (Director) and CF30 (Customer) at Pave Financial Management Limited because he lacked the integrity and the competence and capability to perform those functions. The FSA has also prohibited Mr Hocking from performing any function relating to any regulatory activity.



Among other things, the FSA found that Mr Hocking had made unsuitable recommendations to customers to disinvest from existing arrangements and to invest in unregulated collective investment schemes (“UCIS”).

The FSA had considered that Mr Hocking’s misconduct warranted a fine of £25,000 but since he had provided verifiable evidence that imposing such a financial penalty would cause him serious financial hardship, the FSA instead decided to publish a statement of Mr Hocking’s misconduct.

The FSA also cancelled Pave’s permission pursuant to Part 4A of the Financial Services and Markets Act 2000 (FSMA) to carry on regulated activities for failure to meet the threshold conditions for authorisation. The FSA had concluded that Pave is failing, or is

likely to fail, to satisfy Threshold Condition 5 (suitability) since it did not have competent and prudent management, and Threshold Condition 4 (adequate resources) because, with the withdrawal of Mr Hocking’s approval, the firm would not have adequate human resources to carry on its regulated activities.

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UNITED STATES



WHISTLEBLOWERS

FEWER OPPORTUNITIES SEEN FOR FOREIGN WHISTLEBLOWERS

By Nicolas Morgan and David Sack

According to recent press reports, the US Department of Justice and the Securities and Exchange Commission are conducting two separate investigations into allegations of foreign bribes, one by a major US software company and another by the China bureau of a US newspaper. Both investigations appear to stem from purported whistleblowers located in China – including a Chinese government official and a former employee. The prospect of either of those whistleblowers ever receiving a bounty as a result of the Dodd Frank whistleblower bounty program appears remote at best.

Initial expectations that the Dodd Frank whistleblower bounty program would have broad reach have been tempered by SEC rule-making and recent court cases. When Dodd-Frank was adopted in 2010, some US-based public companies worried that employees “in countries where bribery of government officials has long been a way of life” might circumvent internal company reporting channels in favour of reporting directly to the SEC in pursuit of a bounty. Others, including the Interim Director of Enforcement for the UK’s Financial Services Authority (“FSA”) (now the FCA), “don’t think that financial incentives for whistleblowers would be the thing that significantly changes the effectiveness of whistleblowing”.

While current whistleblower data is too scarce to draw meaningful conclusions about trends, legal developments suggest that would-be foreign whistleblowers face a host of impediments to collecting a bounty, which may reduce the number of foreign tips received by the SEC.

OVERVIEW OF THE SEC WHISTLEBLOWER PROGRAMME

Rewards may pay out on successful actions imposing \$1 million or more in sanctions. Under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank”), the SEC may pay rewards to individuals who provide the SEC with information about a possible violation of the federal securities laws “has occurred, is ongoing, or is about to occur” at companies required to report to the SEC. Specifically, section 922 of Dodd-Frank authorises the SEC to compensate individuals who voluntarily provide original information (ie previously unknown to the SEC) leading to a successful SEC enforcement action resulting in sanctions exceeding \$1 million. The individuals may receive between 10 and 30 per cent of the amount collected in the SEC action or a related action brought by the US Department of Justice, regulatory agencies (eg the Federal Deposit Insurance Corporation), self-regulatory organisations (eg FINRA), and state attorneys general in criminal cases. The whistleblower must provide the information voluntarily, meaning that the whistleblower must not already be required to report the information to the SEC due to a pre-existing legal duty, a contractual duty owed to the SEC or other authority, or a duty arising out of a judicial or administrative order.

REWARDS FOR “ORIGINAL INFORMATION”

The SEC may pay awards when the whistleblower’s original information is “sufficiently specific, credible, and timely” to cause the staff to commence an examination, open or reopen an investigation, or inquire about different conduct as part of a current examination or investigation, any of which leads to the bringing of a successful enforcement action based in part on the whistleblower’s information. Alternatively the SEC may pay rewards where the whistleblower’s original information significantly contributes to the success of an enforcement action regarding conduct that the SEC has already begun to examine or investigate.



WRONGDOERS WELCOME

Culpable whistleblower are also eligible for rewards; however, in determining whether the \$1 million threshold has been satisfied, the SEC will not take into account any monetary sanctions for the whistleblower himself is ordered to pay, or sanctions ordered against entities “whose liability is based substantially on conduct that the whistleblower directed, planned or initiated”. Further, a culpable whistleblower’s assistance will not immunise him or her from SEC actions, as Dodd-Frank and the regulations promulgated thereunder “do not provide amnesty to individuals who provide information to the Commission”.

INTERNAL REPORTING ENCOURAGED

The program also encourages whistleblowers to report possible violations to internal compliance departments. First, it lists interference with internal compliance an reporting systems as a reason for the SEC to consider decreasing a whistleblower’s reward. Second, the SEC gives credit to whistleblowers who report original information through a company’s internal whistleblower, legal, or compliance procedures before or simultaneously with reporting to the SEC. Third, the rule provides a 120 day-window for a whistleblower to report original information to the SEC after first reporting internally.

ANTI-RETALIATION

Finally, the programme protects whistleblowers from employers who might otherwise retaliate against individuals reporting original information to the SEC. Dodd-Frank provides that individuals alleging retaliation may bring a federal course of action for relief, including reinstatement of the whistleblower’s position, twice the amount of back pay otherwise owed the individual, with interest, and attorneys’ fees and costs for bringing suit. Additionally, rule 21F-2(b)(2), promulgated under Dodd-Frank, states that the whistleblower protections codified in Dodd Frank “shall be enforceable in an action or proceeding brought by the Commission”.

NUMBER OF FOREIGN WHISTLEBLOWERS REPORTED BY THE SEC

Thus far, approximately 10% of SEC whistleblower activity in 2011 and 2012 has come from abroad. For both years, by far the largest number of foreign tips came from the UK and China. In terms of subject matter, the single biggest category of tops involved claims of financial reporting misconduct.

Specifically, the number of foreign whistleblower tips, complaints or referrals for fiscal Year 2012 was 324, which comprises 10.8% of the total 3,001 award-eligible tips. Through the SEC’s 2011 Whistleblower Annual Report covered only about two months’ worth of data, it turned out to be a good predictor for 2012. The 2011 Reported listed 32 foreign tips, complaints, or referrals, comprising 11.4% of the total 334 award-eligible tips received for 2011. Whether foreign based tips will continue to comprise 10% of the total may turn in part on the ability of foreign whistleblowers to actually collect bounties. Several legal developments have dimmed prospects for the collection of bounties by foreign whistleblowers.

GROWING IMPEDIMENTS TO FOREIGN WHISTLEBLOWERS

Not all foreign whistleblowing will result in awards. In fact, since adoption of Dodd-Frank in 2010, impediments to foreign whistleblowers collected rewards have increased. Through some restrictions are the result of SEC rule making, others have recently been imposed by developments in case law.

SEC RULES RESTRICT FOREIGN BOUNTIES

The SEC rule-based restrictions on foreign whistleblowers obtaining awards are as follows:

- First, reporting violations of foreign laws will not result in payment. The SEC indicated that the whistleblower program was designed to enhance enforcement of US federal securities laws, and not foreign laws. The SEC limited its program to those



laws it had jurisdiction to enforce. Therefore, “the submission must relate to a violation of the federal securities laws, or a rule or regulation promulgated by the Commission”.

- Second, foreign whistleblowers who first respond to requests by foreign officials before they report to the SEC may not be eligible. Thus, for example, where the SEC requests the assistance of a foreign authority to obtain documents or information, and the foreign authority in turn sends a request to one of its residents, the SEC will not treat the whistleblower submission as “voluntary”.
- Third, foreign whistleblowers who provide information to the SEC may risk criminal penalties for unlawfully disclosing information to authorities outside their own borders. For example, under the China state secrecy laws, a Chinese citizen who provides whistleblower information to the SEC may be subject to punishment “in accordance with the law”. Other jurisdictions, such as France, have so-called “blocking statutes” prohibiting disclosure of financial, commercial, or economic information that might constitute evidence in a foreign proceedings, including SEC investigations. The EC’s award of a bounty will not alleviate the impact of these penalties.
- Fourth, the SEC may provide the whistleblower’s identity to foreign officials without notice to the whistleblower. On the one hand, the SEC states that it will “determine what assurances of confidentiality” it deems necessary before sharing the information with foreign authorities and that it “plan[s] to work closely with whistleblowers on their attorney in an effort to take appropriate steps to maintain their confidentiality,” as required by the rule. On the other, though, the SEC notes that “Congress expressly authorised us to disclose whistleblower-identifying information subject to the limitations... in Section 21F(h)(2)” and concludes that it would be inconsistent with Congressional intent or “the proper exercise of our enforcement responsibilities” to require by rule that the SEC staff notify a whistleblower before any authorised disclosure.

- Fifth, foreign officials, and employees for foreign state-owned entities, are ineligible for SEC whistleblower awards. The SEC excluded foreign officials and employees of state-owned entities because whistleblower awards to these individuals might “create ... the perception that the United States is interfering with foreign sovereignty, potentially undermining foreign government cooperation under existing treaties... incentive[s] for foreign officials to make reports to the United States rather than to local authorities, and concerns about protection of foreign officials who become whistleblowers.”

Recent administrative decisions and case law may further impede foreign whistleblowers’ ability to collect rewards under the SEC’s whistleblower program.

ANTI-RETALIATION PROVISIONS MAY NOT PROTECT FOREIGN WHISTLEBLOWERS

The anti-retaliation provisions of the Sarbanes Oxley Act of 2002 (SOX) may not apply to certain foreign whistleblowers. For example, in late 2011, the Department of Labour’s Administrative Review Board (“**ARB**”) rejected an employee’s challenge to a decision dismissing his case, holding that the SOX’s anti-retaliation provisions “refer only to the violation or implication of domestic securities laws, criminal laws and financial regulation”.

The ARB reasons that employee “did not point to a US law or domestic financial statement that was fraudulent”. The ARB’s decision identified factors for assessing the extraterritorial application of the SOX’s whistleblower provisions, including the nationality of the laws at issue, and the location of the job, company and retaliatory act.



CASE LAW LIMITS THE EXTRATERRITORIAL APPLICATION OF US SECURITIES LAWS

To collect a bounty, a foreign based whistleblower must point to a violation of US federal securities laws. However, the SEC's ability to successfully allege violations against foreign executives has been limited recently in certain respects. If the SEC cannot successfully pursue violations of the US federal securities laws, a whistleblower will collect no bounty.

For example, in February a federal district court judge in Manhattan dismissed the SEC's complaint against a foreign executive in *SEC v Sharef*. The SEC alleged that the executives of a German company paid \$100 million to top government officials in Argentina to win contracts. The court dismissed the executive despite his alleged participation in a telephone call urging others at the company to meet the demands of Argentine officials and make the payments. The judge found that the executive's role in the bribes was "tangential at best", because he neither authorised the bribes, directed the cover ups, nor prepared false financial statements resulting in insufficient "minimum contacts" with the United States to exercise jurisdiction over him.

Another federal district court in February, this time in Chicago, granted defendants' motion for summary judgment dismissing SEC claims *S.E.C. v Bengier*. The SEC charged violations of the federal securities laws against a financial services company's distribution agents and escrow agents, alleging that defendants hired selling agents who targeted elderly citizens in foreign countries and "scammed them through the use of boiler room tactics". Specifically, the SEC alleged that the distribution agents failed to disclose that the commission charged to the investors exceeded 60% of investors' funds leading investors to believe that only nominal transaction fees were charged. In dismissing the claims, the court found that all relevant sale were consummated in Brazil, ie outside of the United States. The court followed recent Supreme Court rulings

that "it is... only transactions in securities listed on domestic exchanges, and domestic transactions in other securities" to which the deferral securities laws at issue apply. Because all purchase agreements were formed outside of the United States, the court concluded that the share purchases were not domestic transactions and that US federal securities laws did not apply.

While neither the Sharef or Bengier cases involved whistleblowers, both represent instances in which the SEC failed in its attempts to apply federal securities laws outside the United States. Such a trend, if it is a trend, may inhibit the willingness of foreign whistleblowers to come forward and will certainly prevent their ability to collect bounties.

In sum, the extraterritorial reach of the SEC's whistleblower program may be more limited than originally imagined, as a result of the SEC's own rulemaking and due to courts' unwillingness to apply US federal securities laws as broadly as the SEC would like.

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FRENCH DRAFT BILL: FINANCIAL AND BANKING REFORM

As a result of the recent financial crisis, the French legislator plans to implement financial and banking reform by adding new provisions to the French monetary and financial code (“MFC”). The French draft bill, released by the Assemblée Nationale, and currently being examined by the French Parliament, is mainly aimed at: (I) implementing a separation of credit institutions’ trading activity; (II) introducing new rules in connection with the prevention and the treatment of credit institutions’ difficulties; and (III) increasing the powers of the French supervisory authorities.

I. SEPARATION OF CREDIT INSTITUTIONS’ TRADING ACTIVITIES

The necessity to guarantee financial stability, the solvency of credit institutions, financial and mixed financial holding companies’ and their capacity to ensure the financing of the economy, several rules have been proposed: the prohibition of proprietary trading and the use of dedicated subsidiaries.

1. Prohibition of proprietary trading

Credit institutions, financial companies and mixed financial holding companies are prohibited to perform the following transactions when their activity of trading in financial instruments exceeds certain thresholds set out by decree, otherwise than by the intermediary of subsidiaries dedicated to these activities:

- trading in financial instruments which involve their own account;
- any transaction entered into by the credit institution for its own account with leverage funds or other funds the features of which are set out by decree of the Ministry in charge of the Economy provided that the credit institution is not secured by a security interest.

However, the new provisions provide for several exceptions to such a prohibition:

- provision of investment services to the clients;
- clearing of financial instruments;
- hedging of the risks of the credit institutions or the group (except in respect of the dedicated subsidiary mentioned above);
- market making;
- careful and healthy management of the working capitals of the group;
- investment transactions of the group.

It has to be noted that the draft bill provides for a specific definition of the terms “provision of investment services to the clients”, “hedging”, “market making”, “investment transactions of the group” for the purpose of the abovementioned exceptions.

The definition of the term “hedging” is likely to be of concern to the industry. According to the draft bill, “hedging” means *“the activity of a [credit institution, financial company or mixed financial holding company] which acts as counterparty in transactions on financial instruments in order to reduce its exposures to risks of any kind in connection with the credit and market activities. The instruments used for such hedging transactions shall be economically linked to the identified risks in accordance with the conditions set out in a decree of the ministry in charge of the economy”*.



2. Dedicated subsidiaries

The dedicated subsidiaries mentioned earlier must be licensed as investment companies or credit institutions. When the subsidiary is licensed as a credit institution, it is not entitled to receive any funds nor to provide any payment services to the clients whose deposits are guaranteed (i.e. cash deposits up to EUR100,000).

These subsidiaries are not entitled to carry out: (i) certain high frequency trading transactions; and (ii) transactions on financial instruments in which the underlying asset is a raw agricultural commodity.

These subsidiaries will have to respect some management rules set out by decree of the Ministry in charge of the Economy. More generally, it is foreseen that a decree will set out the organisation and functioning requirements regarding credit institutions and their dedicated subsidiaries.

The draft bill provides for two dates for implementing the new rules:

- 1 July 2014: audit of the activities to be transferred;
- 1 July 2015: effective transfer of these activities.

The draft bill settles the question of the impact of the implementation on the existing agreements entered into by the credit institutions. According to its current provisions, the transfer of the agreements cannot result in a modification, termination or early repayment of the underlying debts of such agreements.

IMPLEMENTATION OF THE BANKING PREVENTION AND RESOLUTION PROCEEDING

The reform implements a new regime in respect of the resolution and the treatment of credit institutions experiencing difficulties.

1. The Resolution Board of the *Autorité de Contrôle Prudentiel et de Résolution*

The authority in charge of elaborating and enforcing the prevention and resolution measures will be the *Autorité de Contrôle Prudentiel* (French Prudential Supervisory Authority) that will become the *Autorité de Contrôle Prudentiel et de Résolution* (French Prudential Supervisory and Resolution Authority, “ACPR”).

In addition to the existing Board which will become the Supervisory Board and the Enforcement Commission, a special Resolution Board will be created. This Resolution Board is composed of, among others, the governor of the *Banque de France*, the general manager of the *Trésor* and the president of the *Autorité des Marchés Financiers* (the “AMF”).

The financial and banking reform grants new powers to the *Fonds de Garantie des Dépôts et de Résolution* (Guarantee Fund of Deposits and Resolution, the “FGDR”) in relation to the prevention of the insolvency of credit institutions. According to the new provisions, the FGDR can, among others, purchase all or part of the shares of the relevant institution or grant financing to the relevant institution.

2. Recovery, prevention and resolution measures

Credit institutions and investment companies (except for the management companies exceeding a balance threshold which will be set by decree) must draw up and pass on to the ACPR a preventive recovery plan which sets out the contemplated measures to be undertaken in case of a material deterioration of their financial situation. Such a recovery plan cannot include any financial support of the French government or of the FGDR.



The ACPR establishes for credit institutions and investment companies, a preventive resolution plan which sets out specific rules for applying the resolution measures. This plan is considered by the ACPR for a credit institution which is in default.

An institution is in default if there are objective elements evidencing that in the short term it is likely to be in one of the following situations: it does not comply with the capital requirements imposed for the license; it cannot satisfy its payment obligations immediately or in the short term; it requires exceptional support from the government unless such support is a capital grant or a public guarantee of the newly issued liabilities or is made as part of an initiative to respond to a wider deterioration in the economy.

Several resolution measures are set up, to ensure the financial stability and can be taken against any credit institution or investment company. The ACPR have the ability to:

- request any information from the entities subject to its supervision, their directors, their auditors or their employees, which is useful for enforcing the resolution proceeding;
- revoke any liable officer;
- decide the transfer of all or part of one or several branches of activity of the relevant entity;
- depreciate, cancel or convert the share capital and other liabilities in order to absorb the amount of the losses in accordance with a specific priority order set out in the draft bill;
- request from the institution subject to the resolution procedure the issuance of new shares or other instruments related to its capital requirements;
- limit or prohibit the exercise of certain transactions by the institution;

The issue price of the new shares or of other instruments related to the capital

requirements of the institution subject to the resolution proceeding, as well as the sale or transfer price of the shares and of other assets, are determined by an expert but, in case of emergency, the ACPR can make such determinations itself.

Such resolution measures can be taken on a temporary basis without necessarily requiring an adversarial procedure.

It should be noted that according to the current draft bill, the contractual provision according to which the appointment of an interim administrator by the ACPR is deemed to be an event of default will be null and void. In addition, as from the enforcement of the resolution proceeding, the contractual provisions providing for the termination or set-off of the financial obligations cannot be enforced.

EXTENSION OF THE SUPERVISORY AUTHORITIES' POWERS

Both the AMF and the ACPR see their powers enhanced, as well as the *Conseil de Stabilité Financière* ("CSF"). The draft bill also provides for further regulation of French clearing houses.

1. *Autorité des Marchés Financiers*

The AMF is now entitled to request from certain entities (such as authorised investment service providers, entities authorised to provide custody or administration of financial instruments or central securities depositories) any documents or information, whatever their form, which is useful for the purposes of exercising its mission of supervision. The AMF investigators and auditors' powers are enhanced, for instance in case of services delivered via Internet for which they are entitled to use a false identity without being criminally liable in this respect.



2. *Autorité de Contrôle Prudentiel et de Résolution*

The draft bill reinforces the powers of the Secretary-General of the ACPR by enabling him to convene and hear any person subject to the supervision of the ACPR or any person whose hearing is necessary for the purpose of exercising its mission.

New obligations are imposed on credit institutions, investment companies, market undertakings and entities licensed to exercise the activity of custody or administration of financial instruments as well as insurance and reinsurance companies and mutual and provident societies according to which such entities must notify to the ACPR the appointment of their officers in charge and the appointment of any individuals directors. The ACPR will be then entitled to refuse such appointments if it considers that such persons do not meet the conditions of honorability, competence and experience required by their position.

3. Macro-prudential supervision

The draft bill reinforces the prerogatives of the *Conseil de Régulation Financière et du Risque Systémique* (Financial Regulation and Systemic Risk Council) which becomes the *Conseil de Stabilité Financière*. The *Banque de France* together with the CSF watches over the stability of the financial system and contributes to the enforcement of the resolutions of the council.

The CSF ensure the cooperation and exchange of information between the institutions which it represents (such as the AMF and ACPR) and the cooperation with the supervision authorities of the other Member States and the relevant European institutions. It can address to the relevant European institutions any advice for the purpose of recommending the adoption of measures required to prevent any systemic risk threatening the financial stability of France. It can also require from the credit institutions and the investment companies additional obligations in relation to their capital requirements.

4. Clearing houses

The draft bill provides for a revised definition of the clearing house which includes the central counterparties as defined in article 2 (l) of the EU Regulation n°648/2012 (EMIR), the central counterparties and the trade repositories and they must also be licensed by the ACPR and through further consultation with the AMF and the *Banque de France*. Their operating rules are approved by the AMF.

The draft bill adds new provisions in relation to deposits made by the payer to investment services providers, members of a clearing house or made by such members to a clearing house which must take the form of a financial guarantee within the meaning of article L.211-38 of the MFC or any other form sets out by the operating rules. In case of insolvency proceedings opened in France or any similar or equivalent proceedings opened abroad, the creditors of the above-mentioned persons or creditors of the clearing house itself are not entitled to claim any right against the deposits which take the form of a financial guarantee.

In case of the opening of insolvency proceedings against a member of a clearing house or in case of any other event of default in respect of such member, the clearing house can as of right and without any formality:

- transfer to another member, the deposits made with such member and in relation to the positions taken by the non-defaulting clients;
- transfer to another member, the positions registered with it for the account of the clients of such member together with the related deposits;
- take any other action authorised under its operating rules which are likely to limit or eliminate the risks to which it is exposed including, as the case may be, the liquidation of the assets and positions held by the defaulting member for the account of the client.

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FINANCIAL SERVICES TEAM

DLA Piper's dedicated Financial Services team offers specialist legal expertise and practical advice on a wide range of contentious and advisory issues. The team can assist clients on contentious legal matters including: internal and regulatory investigations, enforcement actions and court proceedings in the financial services sector. There is also an experienced advisory practice which gives practical advice

on all aspects of financial regulation, including the need for authorisation, regulatory capital, preparation for supervision and thematic visits, conduct of business issues and financial promotions.

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